Susan Combs Texas Comptroller of Public Accounts

The Texas Community Reinvestment 2009 Update

Keeping Texas communities strong keeps Texas strong. Our role is to monitor the state's community reinvestment strategies including the implementation of programs for small farms and businesses, financial literacy education, disaster relief, affordable housing and other community development initiatives. Collaboration among state agencies, businesses and nonprofit organizations helps transform distressed areas, rebuild infrastructure and create safe and supportive communities for all Texans.

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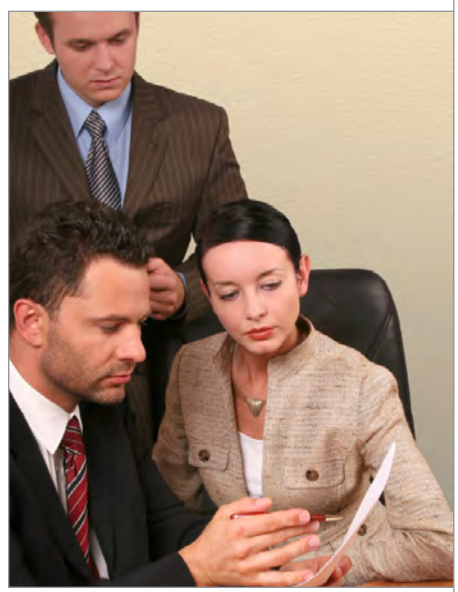
Community Reinvestment in Texas: Update 2009

Executive Summary

The 75th Texas Legislature's House Bill 1414 called for the formation of a state body to work with the financial community in developing statewide community reinvestment strategies. These strategies include using investment pools and other vehicles to leverage private capital from banks, insurance companies and other entities for community projects.

The Community Reinvestment Work Group comprises representatives from the Comptroller of Public Accounts, the Department of Banking (DOB), Department of Economic Development and Tourism (EDT), Texas Department of Insurance (TDI) and the Texas Department of Housing and Community Affairs (TDHCA). Title V, Chapter 395 of the Texas Finance Code requires this group to consult with representatives of the federal Office of the Comptroller of the Currency, the Federal Reserve Board of Governors (FRB), the Office of Thrift Supervision (OTS) and the Federal Deposit Insurance Corporation (FDIC) to identify regulatory changes and initiatives since the previous update in 2007 that affect Texas banks and financial institutions.



The work group monitors and evaluates the state's community reinvestment strategies; ensures that these strategies encourage financial institutions to lend money to low- and moderate-income families and individuals; and coordinates efforts to attract private capital through investments that meet the requirements of the Community Reinvestment Act of 1977 (12 U.S.C. Section 2901 et seq.).

Each biennium, the Community Reinvestment Work Group summarizes the effectiveness of its strategies. The following state agencies contributed to the 2009 update:

- the Texas Department of Banking,
- the Texas Comptroller of Public Accounts,
- the Texas Department of Housing and Community Affairs,
- the Governor's Economic Development and Tourism Division,
- the Texas Department of Insurance,
- the Texas Association of Community Development Corporations,
- the Texas Low-Income Housing Information Service, and
- the Texas Department of Rural Affairs.

The work group met in 2008 to discuss the effectiveness of its current strategies and initiatives and to develop new strategies for 2009 and 2010. The Comptroller's representative collected agency updates from work group members and summarized community reinvestment research from banks, research organizations, advocacy groups and federal regulatory agencies, including the FDIC and the Federal Reserve Bank of Dallas.

This update provides an overview of the Community Reinvestment Act (CRA); describes changes to CRA regulations that have become effective since the 2007 update; highlights recent data and studies on foreclosures and the subprime lending crisis; and describes small business, small farm and community development lending in Texas. The update also outlines state agencies' community reinvestment strategies and provides examples of Texas community reinvestment initiatives.

Recent Legislation

Recent consumer protection bills and legislation enacted by the 80th and 81st Legislatures are intended to assist Texas homebuyers and support community investment. These include:

2009 House (HB) and Senate Bills (SB)

HB 10, added a chapter to the Texas Finance Code titled the Texas Secure and Fair Enforcement for Mortgage Licensing Act of 2009. The new chapter requires mortgage loan originators to register with the Nationwide Mortgage Licensing System and Registry (NMLSR). State mortgage regulators started the National Mortgage Licensing Initiative in 2004 to streamline the licensing process for the mortgage industry and regulatory agencies alike, as a response to the growing number and types of residential mortgage originators. The NMLSR provides a central, standardized system for mortgage licensing.

Recent consumer protection bills and legislation enacted by the 80th and 81st Legislatures are intended to assist Texas homebuyers and support community investment.

The Texas Department of Savings and Mortgage Lending licenses mortgage loan originators employed by credit union subsidiary organizations, which may include organizations owned by one or more credit unions, and provides services such as check cashing, consumer mortgage loan originations and wire transfer services. The Department of Savings and Mortgage Lending will require the Texas Credit Union Department to examine, inspect or investigate subsidiary organizations that are licensed to act as residential mortgage loan originators. Individuals authorized as of July 31, 2009, must register by July 31, 2011. Individuals authorized after July 31, 2009, must register with NMSLR by July 31, 2010.

HB 2450 directs TDHCA to prescribe a form for establishing ownership of residences through nontraditional documentation for title for owners who have applied for disaster recovery housing assistance.

HB 2840 adds a TDHCA representative to the residential mortgage fraud task force and gives TDHCA the ability to share confidential information with other agencies concerned with mortgage fraud in Texas.

HB 4275 gives TDHCA authority to establish separate procedures to implement tax credit-related American Recovery and Reinvestment Act of 2009 (ARRA) funds outside of existing statutory requirements.

HB 4409 directs TDHCA to enter into one or more pre-event contracts for temporary or emergency housing in the wake of a natural disaster.

SB 679 modified the Texas Bootstrap Loan Program to include owner-builder "sweat-equity" requirements, total loan amounts and award limits.

2007 House and Senate Bills

HB 716 established a residential mortgage fraud task force to help track and prosecute mortgage fraud. The task force includes the Office of the Attorney General, the Consumer

Credit Commissioner, the Banking Commissioner, the Credit Union Commissioner, the Commissioner of Insurance, the Savings and Mortgage Lending Commissioner, the presiding officer of the Texas Real Estate Commission and the presiding officer of the Texas Appraiser Licensing and Certification Board. HB 716 also adds Section 411.1407 to the Texas Government Code, authorizing the Credit Union Commissioner to obtain certain criminal history information from the Texas Department of Public Safety.

HB 1038 broadened the Texas Residential Construction Commission's (TRCC's) enforcement powers and changed the definition of "builder." The bill includes in the definition any person who was issued a license by a political subdivision, but not by the state, to practice a trade or profession related to or affiliated with residential construction, as well as persons who perform improvements to home interiors at a cost of more than $10,000. The previous threshold was $20,000.

TRCC must create and maintain an accessible electronic list of registered builders and other builders, including those who build floor plans designed for "mobility-related special needs buyers." The bill also requires a specific written disclosure in each contract for a new home listing the builder's registrations, and establishes new home inspection requirements for unincorporated areas not subject to municipal inspections.

HB 1637 established the "Texas First-Time Homebuyer Program" at TDHCA. Under this program, TDHCA must assist in the origination of single-family mortgage loans for eligible first-time homebuyers. These loans are available to first-time homebuyers with incomes of not more than 140 percent of the area median family income (AMFI) as determined by the U.S. Department of Housing and Urban Development (HUD), and who meet additional requirements prescribed by TDHCA. Buyers with income of not more than 80 percent of AMFI may also be eligible for down-payment assistance.

TDHCA's board must set and collect fees from applicants adequate to cover the expenses of the Program. TDHCA must ensure that a loan is "structured in a way that complies with any requirements associated with the source of the funds used for the loan." The program applies to applications for assistance filed on or after Jan. 1, 2008.

HB 2353 applies the Texas Fair Housing Act to public housing authorities. The bill amends Section 392.006 of the Local Government Code to add the Texas Fair Housing Act to the list of laws with which public housing authorities must comply.

HB 2936 exempts nonprofit community housing development organizations (CHDOs) from the requirements of the TRCC Act if homes or improvements they sell are built by a builder registered under the act; the registered builder contractually agrees to comply with the act's provisions; the registered builder is contractually liable to the homeowner for the act's warranties and building and performance standards; and if the CHDO does not participate directly in the construction or improvement.

HB 3191 exempts certain affordable single-family housing from property taxes. The bill amends Tax Code Section 11.1825 to exempt from property taxation single-family dwellings owned by a charitable organization and built or rehabilitated to be sold to individuals or families whose income does not exceed certain federal median family income thresholds.

SB 99 changed the definition of "*colonia*" throughout state law to require a *colonia* to consist of 11 or more dwellings in close proximity to one another in an area that may be described as a community or neighborhood, in addition to other existing requirements. The bill requires TDHCA and other affected state agencies to require applicants for TDHCA-administered *colonia* improvement funds to submit a classification number for each *colonia* served by the project proposed. The Secretary of State must provide these *colonia* classification numbers.

SB 426 expanded the ad valorem tax exemption for CHDOs. The law allows a property tax exemption granted under Section 11.182 of the Tax Code to continue when the property has been sold at a foreclosure sale and the purchasing organization shows the chief appraiser proof of qualification for the tax exemption within 30 days of the sale.

SB 1733 amended the Government Code to require a lease agreement with a tenant, in developments funded with a housing tax credit allocation, to include applicable federal or state standards identified by TDHCA rule that relate to the termination or nonrenewal of the lease agreement. The bill required TDHCA to adopt rules to this effect by Nov. 1, 2007.

SB 1908 required TDHCA's board to adopt rules governing the administration of the Texas First-Time Homebuyer Program. To be eligible for a mortgage loan, applicants must qualify as first-time homebuyers, have incomes of not more than 115 percent of AMFI or 140 percent of AMFI "in targeted areas," and meet additional requirements prescribed by TDHCA. To be eligible for down-payment assistance, homebuyers must have incomes of no more than 80 percent of AMFI.

The economic downturn of 2008 caused lenders to tighten loan terms, resulting in less credit for most small businesses in the second half of 2008.

The bill also required TDHCA to allocate 95 percent of Housing Trust Fund (HTF) money for non-participating small cities and rural areas, and 5 percent for the benefit of persons with disabilities who live in any area of Texas; to allocate housing tax credits to the at-risk set-aside; and to exempt funds or credits allocated primarily for persons with disabilities. In addition, TDHCA will allocate $3 million in Housing Trust Funds each year from regional allocation and allocate 5 percent in each housing tax credit allocation cycle to developments receiving federal financial assistance through the U.S. Department of Agriculture's Texas Rural Development Office. Funds allocated to developments that involve rehabilitation, the rebuilding of a house on the same lot or the replacement of a substandard unit of manufactured housing must come from funds designated for at-risk developments, projects that have received a rental subsidy, an interest rate reduction, Section 8 housing assistance payment or federal housing equity incentive.

The bill also requires TDHCA to allocate 20 percent or more of the state's low-income housing tax credits in each application cycle to rural areas, with $500,000 or more reserved for each of the 13 uniform state service regions established by the Texas Comptroller of Public Accounts. Any credits that remain must be made available to developments in urban areas within the same state service region before being transferred to any other region.

2009 Community Reinvestment Research Summary

According to the Community Reinvestment Work Group:

- the U.S. lost nearly 3 million jobs in 2008, half of them in the fourth quarter.[1]
- of 763,000 jobs lost in the first two quarters of 2008, more than half were in small firms.

- despite the national economic slump, Texas' 2.1 million small businesses continued to provide the largest source of jobs in the state.
- across most industries in 2007 and 2008, small businesses suffered due to the housing downturn and experienced declines in employment.
- the economic downturn of 2008 caused lenders to tighten loan terms, resulting in less credit for most small businesses in the second half of 2008.
- unincorporated self-employment, including non-incorporated private employers, fell to an average of 10.1 million in 2008, from 10.4 million in 2007, while incorporated self-employment or corporate employment averaged 5.8 million during the same period.[2]
- as of June 2008, the volume of the U.S. Small Business Administration's (SBA's) most popular small-business loan was down 19 percent nationally compared to June 2007. In November 2008, the SBA changed its loan guaranty program to encourage loans to small businesses. Banks may use an alternate base interest rate.[3]

TDI prepares a biennial report on investments made in Texas by life and health insurance companies with $10 million or more in Texas premiums. A total of 280 companies met this criteria in calendar 2007, accounting for about 98 percent of life and annuity premiums collected in Texas in that year.

TDI's biennial report for 2008 shows these insurers made $43 billion in Texas investments in 2007. About 95 percent of the reported investments were in commercial and farm mortgages, political subdivision/public utility bonds and corporate bonds. The largest amounts by category were commercial and farm mortgages ($17.3 billion), political subdivision/public utility bonds ($12.4 billion) and corporate bonds ($10.3 billion).

These amounts, however, are not comprehensive, since many of the companies cannot link their investments to an individual state. This is particularly true of pooled investments. Residential mortgages are frequently purchased through pooled investments, so comprehensive data was not available for this category. In addition, due to the difficulty involved in linking some corporate bond investments to specific states, reporting for that category was optional. Texas investments made by property and casualty insurance companies are also excluded from the totals above because they are not subject to the statute that requires these reports. Additional information about these investments can be found in the *December 2008 Community Investment Report*, available from the Texas Department of Insurance.

Furthermore, Texas law does not require insurers to identify investments by geographic location, except for certain targeted economically disadvantaged areas. Life and health insurers voluntarily reported investments of almost $770 million in the state's economically disadvantaged areas for 2007.[4]

The points below summarize the state agency programs and research included in this report:

- The most recent survey available of community development corporations (CDCs) and community development financial institutions (CDFIs), conducted in 2006 by the Texas Association of Community Development Corporations (TACDC), identified more than $216 million in CDFI loans made to Texas businesses and residents in 2005. Of 259 survey respondents, 210 reported producing affordable housing or planning to do so in 2006 and 2007. Responding CDCs reported building more than 53,000 affordable housing units in 2005, with plans to construct another 5,100 units in 2006 and 2007. TACDC may conduct a new survey in late 2009.[5]

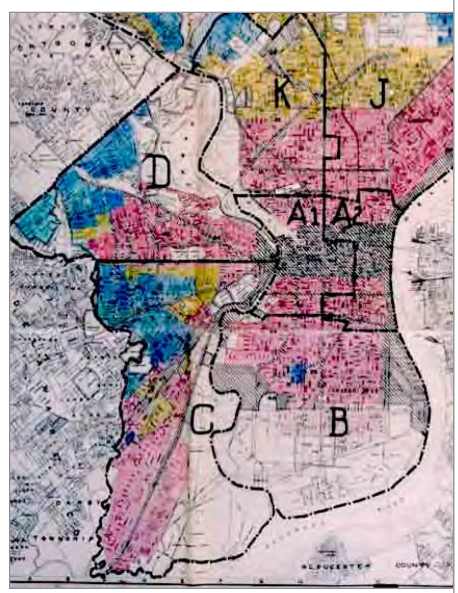
- As of June 2008, the Texas Department of Banking reported the average-sized financial institution operating in Texas managed an estimated $688 million in deposits. Between June 1998 and June 2008, the state's number of branch banking offices rose from 34 to 54 institutions.[6]
- TDHCA administers more than $641 million annually in affordable housing and community assistance programs. Ninety-nine percent of the households served by TDHCA's housing programs in fiscal 2007 were low income, earning no more than 80 percent of the AMFI.[7]
- The Texas Comptroller of Public Accounts partners with approved depository lenders and the Governor's Economic Development and Tourism office on a Linked Deposit Program for loans to minority- and women-owned businesses, child-care centers, nonprofit organizations and small businesses located in state-designated enterprise zones.

The following section of this report update describes the history of the Community Reinvestment Act, as well as changes to the act since the last update in 2007.

Texas law does not require insurers to identify investments by geographic location, except for certain targeted economically disadvantaged areas.

The Community Reinvestment Act

Congress created the CRA (12 U.S.C. 2901), also known as Title VIII of the Housing and Community Development Act, to encourage commercial banks and savings and loans to help meet the credit needs of all segments of the communities in which they operate. The CRA was one of the first federal acts to address "redlining" by banks and savings and loan institutions — the practice of drawing a red line on a map to mark areas where banks will not invest. The term redlining was also used to describe discrimination against people of a specific gender or race despite their geographic location. CRA applies to all federally insured depository institutions, national banks, thrifts and state-chartered commercial and savings banks.



CRA Goals and Community Development

The CRA was intended to improve access to credit for businesses and individuals in low- and moderate-income communities. Since its passage, it has helped affordable housing and community development advocates evaluate the lending performance of CRA-regulated financial institutions while improving home ownership opportunities for underserved populations.

Financial institutions comply with the CRA's requirements by making loans to support:

- construction and rehabilitation of affordable housing;
- financing for multifamily rental property intended for low- and moderate-income persons;
- community development activities of local, state and tribal governments, including financing for geographic areas recovering from natural disasters and distressed or under-served rural counties;
- community development corporations, community financial institutions and minority- and women-owned financial institutions;
- community services for low- and moderate-income individuals, including credit and homebuyer counseling, school savings programs, technical assistance for economic revitalization programs and other activities;
- construction of community facilities in low- and moderate-income areas; and
- environmental cleanup activities and the redevelopment of industrial sites in low- and moderate-income communities.

History of CRA Rules

Amendments to CRA regulations have enhanced the public's access to CRA examination schedules, dollar amounts of community development lending activity, geographic distribution of bank investments, borrower profiles and the number of bank branches in low- and moderate-income areas. These changes also have broadened the options for investment that count as credit toward a financial institution's CRA compliance rating.

In 1989, Congress amended the CRA with the Financial Institution Reform, Recovery, and Enforcement Act. This amendment created four composite CRA ratings to reflect a supervised bank's compliance with the CRA: 1 for outstanding, 2 for satisfactory, 3 for "needs to improve" and 4 for substantial noncompliance. The act also requires public disclosure of CRA examination ratings and written evaluations prepared by regulatory agencies.

A 1991 amendment requires public discussion of regulator evaluations of institutions' CRA performance, to allow community groups to discuss the results with regulators. A third amendment passed in 1992 allows CRA regulators to credit the banks they supervise for investments in minority- and women-owned financial institutions and low-income credit unions.

A 1994 amendment requires institutions with interstate branches to receive a separate examination and rating for each state in which they conduct business. This amendment also requires separate evaluations for banks with branches in any metropolitan area that straddles state lines.

In 1995, Congress further revised the CRA regulations to require separate lending, investment and service tests of regulated institutions, with the lending test carrying the most weight in calculating total CRA credit.[8]

In 2002, the Riegle-Neal Act added Section E to the CRA, prohibiting any bank or branch of a bank controlled by an out-of-state bank holding company from establishing or requiring a branch or branches out of its home state for the primary purpose of taking deposits without planning to make loans in the branch's community.

As financial services institutions continue to consolidate, the total number of community banks dropped from 9,000 in 2005 to 7,000 in 2009. The 7,000 community banks control less than 10 percent of all U.S. bank assets.

The Federal Reserve Board amended the CRA in May 2002 when it approved a final rule to delay the effective date of the Home Mortgage Disclosure Act (HMDA) Regulation C amendments from Jan. 1, 2003 to Jan. 1, 2004. Those amendments expanded coverage of nondepository lenders by creating the $25 million dollar volume test. The volume test measures the quantity of loans made and was added to the existing percentage-based coverage test for non-depository lenders.

As of Jan. 1, 2003, the Federal Reserve Board amended the CRA to require lenders to ask applicants their national origin or race and sex in loan applications taken by telephone. The telephone application rule now also applies to mail and Internet applications.

The asset threshold for depository lenders was raised to $33 million for 2004 data collection and remained unchanged at $10 million or less for non-depository institutions. As of Jan. 1, 2004, HMDA and CRA reporters are required to use the June 6, 2003, geographic statistical area designations provided by the U.S. Office of Management and Budget (OMB) for data collection and reporting in March 2005. The terms metropolitan statistical area, or MSA (used in lieu of metropolitan area) and MetroDiv (Metropolitan Division), became required for HMDA and CRA reporting.

Finally, a 2004 amendment to the CRA requires lenders to collect and report additional data on home loans and financing for manufactured homes, including loan-pricing information and lien status (e.g. secured by a first or subordinate lien or unsecured).

Bank Industry Consolidation, Mortgage Market Growth and the Decline of Community Banks

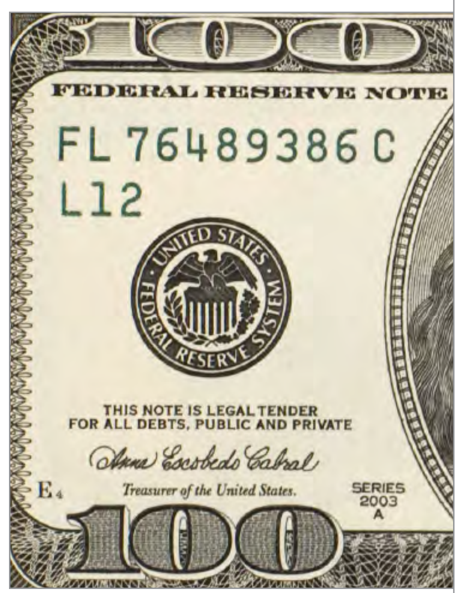
During the mid- and late-1990s, the number of lenders seeking to increase cash flow rose. Lenders began selling primary mortgages to obtain funds to originate new loans.

As the secondary mortgage market grew, financial institutions issued more home mortgage loans. Banks began using credit-scoring software to determine prospective borrowers' ability to repay debts and loans. At the same time, consumers began seeking loans and paying bills through the Internet.

The federal Office of Thrift Supervision (OTS) expanded the category of "small savings associations" in August 2004 to include those with less than $1 billion in assets, regardless of affiliate holding company affiliation.[9]

As financial services institutions continue to consolidate, the total number of community banks dropped from 9,000 in 2005 to 7,000 in 2009. This total includes commercial banks and savings institutions.[10] The 7,000 community banks control less than 10 percent of all U.S. bank assets. Federal Reserve Chairman Bernard Bernanke has identified that small banks can play a key role in fostering the nation's economic recovery, noting that "these banks tend to make direct loans" to individuals and small businesses without becoming involved in complex mortgage-backed securities or complicated derivatives.[11]

Evaluations of Financial Institutions



Federally insured depository institutions, national banks, savings associations, state-chartered commercial and savings banks must comply with CRA regulations. Four separate federal agencies — the FDIC, the FRB, the Office of the Comptroller of the Currency (OCC) and the OTS — evaluate the CRA record of institutions they regulate before approving applications for charters, mergers, acquisitions and branch openings. (See Appendix A for details on the evaluation process and changes to the definition of small banks.)

The FDIC conducts CRA examinations of state-chartered institutions that are not members of the Federal Reserve system. The governors of the Federal Reserve system regulate state-chartered banks that are members of the system, as well as bank holding companies and branches of foreign banks. The FDIC, OCC and OTS examine depository institutions not supervised by the FRB. The FRB considers the CRA record of its member banks before approving applications to open new deposit-taking facilities.

CRA regulation 12 CFR 25 requires the OCC to conduct CRA exams of national banks every three years.[12] It also requires OCC to assess a national bank's record of meeting credit needs in the entire community, including low- and moderate-income neighborhoods, before approving any applications for mergers.

Under CRA regulation 12 CFR Part 563e, OTS must assess a savings association's record of helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods. OTS also must consider that record in evaluating a savings association's application for new branches, the relocation of an existing branch, mergers and consolidations and other corporate activities.[13]

2008 Changes to CRA Rules

On Dec. 17, 2008, federal bank regulatory agencies announced the annual adjustment to asset-size thresholds used to define "small bank," "small savings association," intermediate small bank," and "intermediate small savings association." Asset-size threshold adjustments are determined by the annual November-to-November change in the average of the Consumer Price Index (CPI) for urban wage earners and clerical workers, not seasonally adjusted. The thresholds are used to define small and intermediate small banks or financial institutions.

Following the most recent increase in the CPI index in November 2008, the thresholds for small and intermediate small institutions changed. "Small bank" or "small savings association" now describes an institution that, as of Dec. 31 of either of the two prior calendar years, possessed less than $1.09 billion in assets. "Intermediate small bank" or "intermediate small savings association" describe small institutions with less than $1.109 billion in assets as of Dec. 31 in either of the two prior years, and at least $277 million in assets as of Dec. 31 of both of the two prior calendar years.[14]

The community development test provides banks with opportunities to earn CRA performance credit for making loans to assist infrastructure and building repairs in underserved rural areas, distressed communities and disaster areas.

Regulatory Changes to Asset Thresholds Since 1995

Effective Date	Threshold-Small Institution	Threshold-Intermediate Small Institution
Jan. 1, 2009	$1.109 billion	$277 million
Jan. 1, 2008	$1.061 billion	$265 million
Jan. 1, 2007	$1.033 billion	$258 million
Sept. 1, 2005	$1 billion	$250 million
July 1, 1995	$250 million	N/A

Note: Since July 1, 2007, institutions regulated by the OTS have had the same asset threshold as listed above for Jan. 1, 2007.
Source: Federal Financial Institutions Examination Council.

The CRA exam for intermediate small banks (ISBs) includes a community development test and a lending test. The community development test examines the bank's activities that address the community development needs of its service area, including the number and amount of community development loans and qualified investments and its "responsiveness" to local community development needs. The bank's responsiveness is measured by the number and value of loans it issues for affordable housing and community services targeted to low- or moderate-income individuals as well as lending focused on economic development and rebuilding of low- and moderate-income neighborhoods.

The community development test provides banks with opportunities to earn CRA performance credit for making loans to assist infrastructure and building repairs in underserved rural areas, distressed communities and disaster areas. The 2005 changes did not affect thrifts regulated by the Office of Thrift Supervision. In the case of ISBs, OCC regulators continue using the streamlined lending test and the community development test. They judge an ISB on its business strategy, bank capacity and the community development needs of its local service area. The community development test does not consider retail banking services and does not review a bank's record of opening and closing branches.[15]

An ISB may choose to be evaluated by the OCC as a large bank under the three-part lending, investment and service test if the bank collects and submits required loan data outlined in regulation 12 CFR 25.21(a)(3). The lending test evaluates five performance criteria including loan-to-deposit ratio, lending in and out of the assessment area, responses to complaints, geographic distribution of loans and borrower distribution of loans.[16]

The OCC examines banks on a cycle determined by the bank's asset size and performance on previous examinations. Banks with more than $250 million in assets fall in a cycle that starts 36 months after the bank's previous OCC examination. Under the Gramm-Leach-Bliley Act, the OCC follows an extended exam cycle for small banks with aggregate assets of $250 million or less and an overall "outstanding" CRA rating. OCC exams of small banks with an overall CRA rating of "satisfactory" cannot begin sooner than 48 months after their most recent exam, and no earlier than 60 months after their last CRA exam if the bank was ranked "outstanding" on its last exam. The OCC may remove banks from the extended exam cycle when they apply for a depository facility or for reasonable cause.

Under the 2005 CRA rules, a bank must receive a "satisfactory" on the community development and lending tests before it can obtain approval for new branches or affiliates. The community development test analyzes four areas of bank activity:

- affordable housing;
- community services;
- economic development and revitalization; and
- stabilization activities.

The affordable housing and community services evaluations apply to a bank's lending to low- or moderate-income individuals. The economic development evaluation applies to a bank's lending to small businesses and farms, while the revitalization or stabilization test evaluates bank services provided to low-or moderate-income census tracts or underserved rural areas. OCC's community development definition includes activities that stabilize designated disaster areas and "underserved and distressed" rural areas.[17]

Office of Thrift Supervision

The Office of Thrift Supervision monitors data collection and reporting for the small banks it regulates. OTS collects data and reports from all savings associations except for small institutions — thrifts with less than $1 billion in assets as of Dec. 31 of either of the prior two calendar years.[18] OTS applies a streamlined examination under CRA regulations for "small institutions," which analyzes the institution's lending record.[19]

In 2005, FDIC, FRB and OCC issued a final rule that differed in several ways from the OTS rule. Their final rule created a new community development test for intermediate small banks with assets between $250 million and $1 billion; provided criteria for evidence of discrimination or practices in violation of laws, rules or regulations that could hurt an institution's CRA rating; adjusted regulated institutions' asset thresholds annually for inflation as measured by the CPI; and tightened CRA exam choices for large banks in the areas of lending, investment and services by maintaining weight allocations of 50 percent on lending, 25 percent on investments and 25 percent on services.

As of July 1, 2007, OTS aligned its CRA regulations with those of other federal banking regulatory agencies for exams beginning in the third quarter of 2007.[20]

Lending institutions of any size can choose to develop a strategic plan instead of being examined by regulators. The strategic plan option allows the institution to structure its CRA evaluation criteria and objectives to meet the unique needs of the community it serves, based on its own lending capacities, banking strategies and expertise.

Under the CRA, regulatory examiners evaluate large banks once every two years to grade their lending, investments and services in low- and moderate-income neighborhoods. Large bank examinations are based on lending, investment and service performance and must disclose data on mortgage lending in non-metropolitan areas, community development activities and loans to small businesses. An unsatisfactory or weak CRA record can result in the denial of a financial institution's request to expand.

Examiners can customize federal regulatory tests to examine limited-purpose and wholesale banks that specialize in large commercial deposits and provide credit cards but do not make home loans or accept small deposits. Customized tests focus on the number of community development loans and investments, including low-income housing tax credits or investments in small businesses that a bank has made in its service area.

The four federal regulatory agencies publish lists each quarter of CRA examination schedules for regulated banks and savings institutions. Regulators maintain the lists on their agency Web sites and provide them to the public.

CRA and the Financial Services Industry

The financial industry changed in many ways following the 1997 passage of the CRA. These changes include consolidation of large and small banks, deregulation of the banking industry, shifting market forces and technological advances.

Mortgage banking companies, without traditional banking regulatory oversight, grew in number and became more involved in the financial and insurance services sectors, making loans without traditional banking regulatory oversight.

Competition has benefited banks and other financial institutions. Check-cashing and credit-card services, the marketing of insurance products and sales of securities across state lines also have had an impact. Mortgage banking companies, without traditional banking regulatory oversight, grew in number and became more involved in the financial and insurance services sectors, making loans without traditional banking regulatory oversight.

CRA and the Gramm-Leach-Bliley (GLB) Act

The 1999 Gramm-Leach-Bliley (GLB) Act repealed restrictions found in sections 20 and 32 of the Glass-Steagall Act of 1933 concerning the affiliation of banks and securities firms. Known as the Financial Services Modernization Act of 1999, the GLB Act created new forms of financial institutions called "financial holding companies" as part of section 4 of the Bank Holding Company Act.[21]

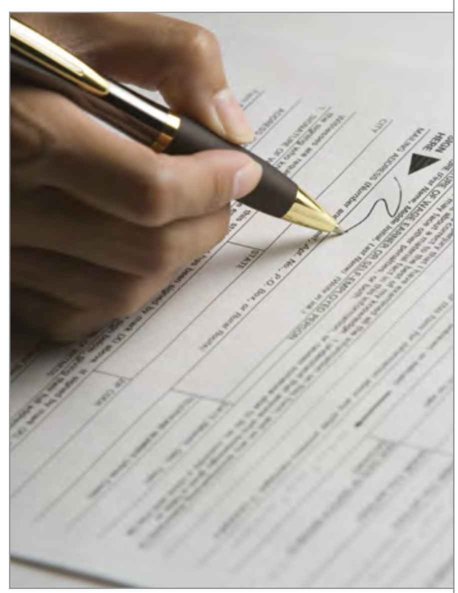
The GLB Act requires that financial holding companies, insured depository institutions affiliated with a financial holding company and stand-alone insured depository institutions can be approved for expanded activities or acquisitions only if their latest CRA examination rating is satisfactory or better.

The GLB Act also created a system for federal and state financial regulatory compliance, requiring the Federal Reserve Board to supervise financial holding companies. For example, the Texas Department of Banking regulates the state's banks following compliance guidelines issued by the FRB. The act also ended legal barriers among the banking, insurance and securities industries, allowing them to combine services and provide various financial products. Under the GLB Act, state insurance departments regulate the insurance activities of banks and all financial firms involved in the business of insurance.

The GLB Act also reduced the frequency of regulatory examinations for small banks with passing CRA ratings. Small banks with outstanding ratings are evaluated once every five years, and once every four years if they pass with a satisfactory rating. Regulatory agencies may examine small banks more frequently if they believe they have a compelling reason to do so.

Regulatory examiners use the Federal Financial Institutions Examination Council's (FFIEC) revised interagency examination procedures to assess institutions' compliance with the CRA "sunshine requirements" of the GLB Act. These requirements apply to the funds of an insured depository institution or any affiliate with an aggregate value of more than $10,000 in a calendar year. The provisions cover written agreements made in compliance with the CRA that involve funds or other resources of an insured depository institution, including any affiliated institutions, with an aggregate annual value of more than $10,000. Regulatory examiners also apply the CRA sunshine requirements to financial institutions having loans with aggregate principal value of more than $50,000 in a calendar year.

The sunshine requirements do not cover any agreement with a nongovernmental entity or person that has not had a CRA contact with an insured depository institution or affiliate or a banking agency. This includes agreements entered into by entities or persons that solicit charitable contributions or other funds without regard to the CRA. Parties to covered agreements must disclose the agreement to the public and the appropriate agency. All parties must file a report with the appropriate regulatory agency each year.[22] When management determines that a financial institution is a party to one or more covered agreements, the regulation requires examiners to investigate and describe the institution's covered agreement disclosure practices.



Home Mortgage Disclosure Act Data Disclosure

The federal Home Mortgage Disclosure Act (HMDA) of 1975 requires most mortgage lenders in metropolitan areas to collect data on their housing-related lending activity and report the data to the Federal Reserve Board to the attention of the regulatory agency under which they report annually. HMDA reporting makes the data available to the public.

HMDA data requirements apply to home improvement loans, purchases and refinancings. Under the CRA, agencies that evaluate insured depository institutions must use HMDA data when evaluating regulated institutions' records of meeting community mortgage credit needs.

- Initially, HMDA was used to help determine whether financial institutions were serving the housing needs of their communities and to enforce fair lending practices. Combined with the Federal Reserve Board's Regulation C, HMDA requires the majority of depository institutions and certain for-profit, non-depository institutions to collect, report and disclose data concerning home purchase and improvement loans, refinancing and related loan applications.
- Congress changed HMDA in 1989 to require lenders to collect data about denied home loan applications and related applicant or borrower information.
- The Federal Reserve Board amended HMDA Regulation C in 2002 to require new data fields and price information for certain loans. HMDA requires lenders to indicate whether a loan or application involves a one- to four-family home, a multi-family residence or a manufactured home. The institutions must report the type, purpose and amount of the loan; the property's location; and the applicant's ethnicity, income, race and sex. HMDA data requirements include most home-secured loans except for home equity loans for credit card debt consolidation and

medical expense payments. Regulations make reporting of home equity lines of credit (HELOCs) financing optional.

- From 1989 through the 1990s, national community development groups successfully pursued reforms of the HMDA that were intended to increase the amount of disclosed information required on loans. Recent reforms included the Financial Institutions Reform, Recovery and Enforcement Act of 1989, which added new data disclosure requirements. In 2002, the FRB revised Regulation C to require lenders to disclose data on loans covered by the Home Ownership and Equity Protection Act including data on home loans, lien status, loan pricing and whether an application or loan involves a manufactured home.
- As of Jan. 1, 2007, the FRB increased the asset-size exemption for banks, consumer finance companies, credit unions, mortgage companies with offices in metropolitan areas and savings and loan associations. Lenders with $36 million or less on Dec. 31, 2006, did not have to collect or report data under HMDA in 2007.[23]
- In 2008, the Federal Reserve Board adjusted the asset-size exemption threshold to $39 million, exempting depository institutions with fewer assets as of Dec. 31, 2008, from collecting HMDA data for 2009.[24]

The FRB also amended HMDA Regulation C as of Oct. 1, 2009, to revise the rules for reporting price information on high-priced loans. The revised rule requires lenders to report the spread between a loan's APR and a survey-based estimate on APRs currently offered on comparable prime mortgage loans when the spread equals or is greater than 1.5 percentage points for a first loan or 3.5 percentage points for a subordinate-lien loan. Labeling the loan as adjustable or fixed also has been added as a required element in the rate spread calculation. As of the same date, reporting of price information compliance is mandatory for loan applications and for loans that close on or after Jan. 1, 2010, regardless of application dates.

The FRB also amended HMDA Regulation C as of Oct. 1, 2009, to revise the rules for reporting price information on high-priced loans.

Metropolitan Statistical Area Boundaries and HMDA

Both the CRA and HMDA use the U.S. Office of Management and Budget's (OMB's) statistical area definitions. In 2003 and 2004, these definitions changed, which affected HMDA loan data collection and reporting by financial institutions located within OMB's revised statistical areas.

OMB's revised definitions created 49 new metropolitan statistical areas, changed the boundaries of many other MSAs and established new types of statistical areas including metropolitan divisions (MetroDivs or MDs). New OMB statistical areas also include combined statistical areas and micropolitan statistical areas. OMB eliminated the terms "Consolidated MSA" (CMSA) and "Primary MSA" (PMSA). Only MDs and MSAs are recognized for CRA and HMDA reporting purposes. Micropolitan areas and "nonclassified" areas are considered "nonmetropolitan" for all purposes under HMDA and CRA.

- As of Jan. 1, 2004, FFIEC required affected financial institutions to collect HMDA and CRA data using the OMB's new definitions. Collected data must include the property location using an MSA or MD code if the property is located in an MD. (For detail of OMB changes affecting HMDA, see Appendix B.)
- CRA and HMDA reporting institutions began using OMB's new geographic designations in collecting loan data in 2004.
- For loan applications in metropolitan areas, a property's MSA or MD must be reported, rather than the metropolitan areas (MAs) required in 2003. When

- lenders report an MSA that has been subdivided into MDs, the lender will report both the MD and MSA when the properties have not been subdivided.
- CRA and HMDA reporting institutions began reporting property location using MSA or MD codes on January 1, 2004, when the property is located in a MD.

Home Equity Lines of Credit in Texas

In 2003, Texas voters authorized two amendments to the Texas Constitution that permit lenders to provide HELOCs to Texas homeowners and allow refinancing of home equity loans with reverse mortgages. Most lenders provide lower interest rates on a HELOC than on unsecured loans. Interest paid on a HELOC can be deducted from federal income taxes.[25]

A traditional home equity loan is offered for a specific time period, with repayment of interest and principal required in equal monthly payments at fixed interest rates. Home equity loans may have a value of up to 80 percent of the market value of the home, after deducting any loans secured with the home itself, and can be used as needed for any type of expense. A HELOC, by contrast, is a revolving account that allows the homeowner to borrow from time to time up to a certain credit limit.[26]

- Banks and finance companies report HELOCs as receivables on quarterly Call Reports, while mutual savings banks report HELOCs on Federal Reserve Call Reports.
- The financial services industry, the U.S. Census Bureau and the Federal Reserve Board collect and report HELOC data.
- Federal savings banks and savings and loan associations report credit line receivables on Call Reports.
- Finance companies report commercial and residential mortgages without separating HELOCs from traditional loans.[27]

Federal Economic Stabilization Funding and the CRA in the United States (U.S.) and Texas

On Feb. 13, 2009, Congress enacted the American Recovery and Reinvestment Act of 2009 (ARRA), more commonly known as the federal stimulus legislation. The ARRA provides $53.6 billion for the states in its State Fiscal Stabilization Fund under Title XIV. The ARRA will provide the Texas Department of Housing and Community Affairs and the Office of Rural Community Affairs millions of stimulus dollars for community reinvestment.

TDHCA will receive $150 million for home rental assistance, housing search and credit repair activities, as well as case management and other expenses. The Texas Department of Rural Affairs (TDRA) will receive $19.5 million in grant funding for water, wastewater and other Texas infrastructure-related projects. The funds will help strengthen local economies throughout the state by supporting job retention and affordable housing construction projects, among others. The stimulus funds will be used to hire engineers and construction workers and to purchase concrete, electrical wiring and building supplies.

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The CRA: 30 Years of Impact

During the more than three decades since the CRA became law, critics and supporters alike have debated its impact. Critics claim that the CRA increases regulatory and data reporting requirements for regulated financial institutions while encouraging banks to make unprofitable and risky loans. Supporters argue that the CRA promotes responsible lending and lines of credit in low- and moderate-income communities, where economic activity is often needed due to relatively low property values, low numbers of comparative property appraisals and reduced liquidity.[28]

Banks and savings and loan institutions issued most home purchase loans when the CRA was passed in 1977. Between 1977 and 2006, the CRA fostered homeownership lending by providing access to credit for low- and moderate-income persons through CRA-regulated institutions. During this 30-year period, bank activity in low-income communities rose as CRA regulations evolved.

CRA advocates say progress has been made. In addition to an estimated $5 trillion in investments, the CRA has helped stimulate the provision of loans and services in low- and moderate-income areas over the last 30 years.

In addition to an estimated $5 trillion in investments, the CRA has helped stimulate the provision of loans and services in low- and moderate-income areas over the last 30 years.

Between 1996 and 2006, community development loans increased by almost 220 percent, from just under $18 billion to more than $56 billion. During this period, low- to middle-income neighborhoods' depository institutions made more than 12 million business loans with a cumulative total of $513 billion. Supporters continue to recommend refinements to CRA regulations to address the impact of consolidation in the financial services and previously unregulated home mortgage lending industries. Following the 2005 hurricane disasters along the Gulf Coast, CRA supporters directed much of their attention to financial industry rule changes aimed at stimulating economic activity through community development lending in all areas, not only urban centers. The OTS changed its definition of community development used for savings associations to conform to that of the FRB, OCC and the FDIC's final rule for banks of August 2005. As a result, OTS' April 12, 2006, ruling encouraged savings associations to increase community development loans and services and qualified investments in nonmetropolitan middle-income areas and areas affected by disasters.

CRA supporters studying the CRA's impact recently identified steps needed to modernize the law and apply it to non-bank financial institutions. Some actions would broaden capital and credit access for minorities in low- and moderate-income areas. Specifically, the suggested CRA policy changes include:

- extending the CRA to non-depository institutions, credit unions, mortgage companies, insurance firms, investment banks and securities firms;
- creating rigorous transparency requirements to expose illegal and predatory lending practices and to penalize discriminatory lending practices with lowered CRA ratings;
- evaluating small banks as frequently as large banks;
- revising CRA assessment areas and including non-depository bank affiliates in CRA exams;
- refining CRA examination criteria to include separate evaluations of purchases, loan originations, prime and high-cost lending; and
- ensuring that CRA exams identify lending, investments and services to minority borrowers and communities.[29]

Small-Business, Small-Farm and Community Development Lending in the U.S. and Texas

This section examines the recent status of small-business, small-farm and community development lending in the U.S. and Texas. The Comptroller's office reviewed data collected by the Federal Financial Institutions Council (FFIEC), the U.S. Department of Labor and the U.S. Small Business Administration. The SBA's Office of Advocacy defines "small business" as an independent business having fewer than 500 employees. According to the SBA, the U.S. had about 27.2 million small businesses in 2007. Almost six million of these had employees. Small businesses with fewer than 500 employees:

- represent about 99.9 percent of all U.S. employers;
- employ 46.8 percent of the Texas work force;[30]
- generate half of all U.S. nonfarm private output and produce 52 percent of private-sector output;[31]
- comprise more than 93 percent of businesses in every state;[32]
- create more than half of all jobs in the U.S.;
- contribute more than 50 percent of nonfarm private gross domestic product;
- pay 45 percent of total U.S. private payroll; and
- make up more than 97 percent of the total number of identified exporters in the U.S.

During the last decade, small firms generated between 60 to 80 percent of net new jobs annually in the U.S. and employed more than 40 percent of the country's high-tech workers (scientists, engineers and computer workers).[33] Small firms create the majority of new jobs, fuel competition and innovation and fill niche markets.

SBA research indicates that the number of new small firms is the single most important factor in growing gross state product, state personal income and total state employment.[34]

Because of their economic importance, banking analysts, legislative affairs groups, state and federal regulatory agencies and small-business advocates continue to examine the factors affecting small businesses and their access to capital and credit.

Across the U.S.

Each year, FFIEC collects loan data reported by CRA-regulated entities with assets of $250 million or more, as well as institutions of any size if owned by a holding company with assets of $1.033 billion or more. This includes small-business, small-farm and community development loan data. The maximum small-business loan size reported is $1 million; the maximum small-farm loan size reported is $500,000.

A total of 998 lenders reported CRA data on small-business, small-farm and community development lending in 2007. This information came from 771 commercial banks and 227 savings institutions. FFIEC found the average small-business loan was about $24,400 and the average small-farm loan was about $59,800. About 96 percent of the small-business loans and 83 percent of the small-farm loans were for amounts of less than $100,000. An estimated $329 billion was loaned through 13.5 million small-business loans; $13.1 billion was loaned through 219,000 small-farm loans.

2007 CRA Data
Loans to Small Businesses and Small Farms in the U.S. With Revenues of $1 Million or Less
(Lenders Reporting to the FFIEC = 998)

Description	Small Businesses	Small Farms
Total Dollars Loaned	$ 329	$ 13.1 Billion
Total Number of Loans	13,500,000	219,000
Average Loan Amount	$ 24,400	$ 59,800
Percentage of Loans to Businesses with Less than $1 Million in Revenues	38%	81%
Percentage of Loans Under $100,000	96%	83%
Percentage of Loan Originations and Purchases by Large Commercial Banks & Savings Associations with Assets of $1.033 Billion or More	90%	>50%

Source: Federal Financial Institutions Examinations Council.

According to Equifax research data on 25 million small businesses, commercial bankruptcies almost doubled between March 2008 and March 2009.

The 2007 CRA data indicate 38 percent of reported small-business loans and 81 percent of small-farm loans were made to businesses with revenues of $1 million or less.

FFIEC found that 38 percent of small-business loans made in 2007 were to small firms, compared to 47 percent in 2005 and a high of 60 percent in 1999. Changes in bank data collection practices and renewals with higher credit limits may factor into the reduced lending to small businesses seen in the years before the 2008-2009 recession. Also, small-business loans made by banks may go unreported since a number of banks no longer collect revenue-size data from business loan customers.

Of small-business loans reported under the CRA, 88 percent were concentrated in principal city and suburban areas, while 60 percent of the small-farm loans, as measured by the number and dollar amount, were made in rural areas.

The number of community development loans fell among reporting CRA institutions for 2007. An estimated 75 percent of reporting banks made community development loans; the number of reporting institutions, however, slipped by 2 percent, to 746, from 813 in the previous reporting period. The reduced loan report figures were due to changed CRA rules that exempt institutions with assets of less than $1.033 billion from reporting. Consistent with reporting for 2006, lenders with $1.033 billion or more in assets made the largest number of community development loans in 2007.[35]

According to Equifax research data on 25 million small businesses, commercial bankruptcies almost doubled between March 2008 and March 2009. For example, the Dallas-Plano-Irving area recorded 162 commercial bankruptcy filings in March 2009, up from 73 in March the previous year. In contrast, the Amarillo metro area made the bottom 15 list of cities in Texas with the fewest small-business bankruptcy filings during the same 12-month period.[36]

In Texas

According to the SBA Office of Advocacy, small businesses are the single largest source of new employment growth in Texas, providing thousands of new jobs for minorities and women. Nationally, small businesses create two out of every three new jobs.[37] Small businesses include small employers with fewer than 500 employees, large employers with 500 or more employees and nonemployers, which are businesses that operate without employees. As of 2006, the SBA Office of Advocacy estimated Texas had 2.1 small businesses based on U.S. Census Bureau data, including 386,100 small employers, 5,100 large employers and 1.7 million nonemployers. The health care and social assistance industry accounted for the state's largest number of small-business employers in 2006.[38]

The Community Reinvestment in Texas Work Group's research of small-business turnover in Texas found that business bankruptcies declined to 2,480 in 2007, from 3,590 in 2005, and that the health care and social assistance industry was the state's largest small-business employer in 2006.

Financing Small Business in the U.S. and Texas

Research published by SBA since the 2007 update continues to show that large lending institutions dominate the commercial, industrial and small-business lending markets. The SBA Office of Advocacy found that angel investment funds are the largest source for seed and startup capital.

More than 50 percent of Texas small businesses obtain capital from commercial bank loans. The other half secure their funding through various financing methods, mostly from small local commercial lenders. Small-business startups often begin with the equity of individuals, nonprofit organizations and venture capital funding.[39] Venture capital includes investments in private, young and fast-growing companies.

Research released by the SBA Office of Advocacy shows that large banks in the U.S. made 38 percent of small business loans under $1 million in 2005. Between June 2006 and June 2007, the total number of small-business loans rose by 15 percent. Loans for less than $100,000 rose by 13.7 percent during the same period. In June 2007, total small-business loans for less than $1 million amounted to $685 million out of the $2.02 trillion in business loans issued.

In the U.S., commercial banks provide more than 80 percent of credit-line loans for small businesses. In Texas, both commercial banks and savings and loan institutions make loans to small businesses.

While credit conditions appeared to support U.S. small-business financing in early 2007, the downturn in the housing market and rising energy prices depressed net borrowing compared to 2006. Accelerated borrowing by government and nonfinancial businesses helped mitigate the heavy fall in home mortgage borrowing that year. Small-business financing rose through June 2007 for all loan sizes and especially for loan amounts between $100,000 and $1 million. Large financial institutions with at least $10 billion in assets made more than half of all loans for less than $100,000 in the U.S. small-business financing market in 2007.[40]

Community Development Lending Across the U.S. and Texas

Under CRA guidelines, community development loans provide support primarily for affordable housing for low- or moderate-income persons and community services for these populations, including activities that encourage economic development through small-business or small-farm loans. Community development corporations and community development financial institutions use these loans to revitalize low- and moderate-income communities.

Rural Areas Benefit from Definition of Community Development

The 77th Texas Legislature created the Office of Rural Community Affairs, which was renamed Texas Department of Rural Affairs (TDRA) in 2009, to serve as the state's central agency for rural health, economic development and community development programs. TDRA is the federally designated State Office of Rural Health and the state's lead agency for disaster recovery funding from the U.S. Department of Housing and Urban Development.

Following the devastation left by hurricanes Katrina and Rita in 2005, federal banking and thrift regulatory agencies revised the CRA regulations. Banks now can offer their CRA assessment areas more options for investments, services and loans. Revitalization or stabilization activities must help distressed or underserved nonmetropolitan middle-income geographies based on poverty rates, loss of employment and population density. The Office of the Comptroller of the Currency (OCC) defines middle-income geography as a Census-defined census tract in which individual income is at least 80 percent and less than 120 percent of the area median income. These changes allow national banks to receive CRA credit for investments in communities affected by either of the two hurricanes, whether they are in their assessment areas or not. Examples of investment options include:

- affordable housing for low- and moderate-income persons.
- bank activities in rural areas that help stabilize or stimulate federally designated disaster areas.
- financing for new septic lines for low- and middle-income individuals.
- community services for low- or moderate-income persons.
- disaster recovery, including new house construction and house and manufactured housing repairs, to attract new businesses and residents and retain existing ones.
- loans for small-business or small-farm activities that stimulate designated disaster areas or defined non-metropolitan, middle-income areas that are underserved or distressed. This applies to geographic areas in which median family income is at least 80 and less than 120 percent of the area median income.[41]

The Texas Department of Rural Affairs and the Texas Community Development Block Grant Program

In Texas, several agencies are responsible for community and economic development programs and initiatives. The 2001 Texas Legislature created the Office of Rural Community Affairs, which was renamed Texas Department of Rural Affairs in 2009, to serve as the state's central agency for rural health, economic development and community development programs.

TDRA is the federally designated State Office of Rural Health and the state's lead agency for disaster recovery funding from the U.S. Department of Housing and Urban Development. The agency manages nonhousing awards for hurricanes Ike and Dolly and also monitors government actions that affect rural Texas.

The agency includes a program compliance and audit unit; a research, policy and development unit; a community development block grant program unit; the Texas State Office of Rural Health; a disaster recovery unit; and an outreach and special services unit that includes experts on rural emergency services.

TDRA's *Texas Community Development Block Grant Program* (TxCDBG) is the nation's largest. The federal Department of Housing and Urban Development (HUD) awarded the program $73,017,739 for program year 2009.[42] The program serves 1,017 HUD-designated nonentitlement cities and 245 HUD-designated nonentitlement counties or rural communities. Nonentitlement cities are cities with populations under 50,000. Nonentitlement counties are counties with fewer than 200,000 persons in the nonentitlement cities and unincorporated areas in the county. The TxCDBG program provides services to more than 480,000 Texans annually.[43]

The program focuses on providing basic human needs and sanitary infrastructure to small, rural communities. Local needs eligible for financial assistance include clean drinking water, sanitary sewer systems, disaster relief and urgently needed projects, including housing, drainage and flood control, navigable streets, economic development, community centers and other related activities.

All proposed activities must meet one of the following three HUD National Program Objectives:

- principally benefit low- and moderate-income persons;
- aid in the elimination of slums; or
- meet other community development needs of particular urgency that represent an immediate health or safety threat to community residents.

The program's primary objective is to develop viable communities by providing decent housing, suitable living environments and economic opportunities. The following table identifies the amounts and purposes of funds administered by the TxCDBG Program.

Texas Community Development Program
2009 CDBG Funding Summary

Fund	Amount
Community Development Fund	$45,059,247
Texas Capital Fund	$10,594,874
Colonia Planning and Construction Fund	$5,301,774
Colonia Economically Distressed Areas Program (EDAP) Fund	$2,000,000
Colonia Self-Help Centers Fund	$1,825,443
Disaster Relief/Urgent Need Fund	$2,993,727
Planning and Capacity Building Fund	$657,160
Small Towns Environment Program	$2,294,982
Renewable Energy Demonstration Pilot	$500,000

Deobligated and/or program income of $500,000 made available the first day of program year 2009. Deobligated funds are program funds unused by grantees and returned to TDRA. Program income refers to income generated from the use of CDBG funds returned to TDRA.
Source: Texas Department of Rural Affairs.

The Community Development Fund is the largest fund in the Texas CDBG program. Every biennium, eligible cities and counties may apply through a regional competition for Community Development Fund assistance. Eligible activities include infrastructure projects such as drainage, sewer and water system improvements, housing rehabilitation and improvements to bridges and streets. Each of the 24 state planning regions receives an allocation each year based on its population, poverty and unemployment levels.[44]

TDRA and Regional Review Committees (RRCs) share the process of scoring applications for the Community Development Fund. The RRCs consist of 12 local officials appointed by the governor for two-year staggered terms. Their role is to help set regional priorities for projects funded through the Community Development Fund and to develop scoring criteria for them. The RRCs hold meetings in each of the 24 regions to develop scoring criteria and regional priorities. The scoring process allows RRCs to determine the majority of the total score, while TDRA's score is 10 percent of the maximum possible score for each RRC. For the 2009-2010 biennium, the scoring was modified to accommodate new, objective scoring criteria required by HUD.[45]

Texas CDBG Program Funds

TDRA's *Small Towns Environment Program* is a community development fund that encourages the community's residents to help themselves by committing local volunteers, donating their own time and resources and providing available equipment for the construction of water or sewer projects.[46]

The *Planning and Capacity Building Fund* provides assistance for planning activities that assess local needs. This fund also supports the development of strategies to address local needs, to build or improve local capacity, including hiring professionals who help plan and develop community revitalization projects. Related projects may include the installation of broadband and telecommunications infrastructure.[47]

TDRA designated up to $500,000 in 2009 Community Development Block Grant funds to help eligible rural communities install their own renewable energy projects.

While TDRA focuses most of its efforts on eligible rural communities statewide, several funds are directed specifically to the *colonias*, economically depressed, unincorporated residential areas along the Texas-Mexico border. About 400,000 Texans live in *colonias* that lack potable water, sewage systems, electricity, paved roads and sanitary housing.[48] Funds directed to county applicants for projects in these areas include the *Colonia Construction Fund*, *Colonia Economically Distressed Areas Program Fund* and the *Colonia Self-Help Centers Fund*.

The *Colonia Construction Fund* targets assistance to *colonias* located within 150 miles of the Texas-Mexico border. The fund is used primarily to construct safe, sanitary and cost-effective water and sewer facilities for *colonias* that lack basic infrastructure.[49]

The *Colonia Economically Distressed Areas Program Fund* is used to provide assistance to colonia areas connecting to a water and sewer system improvement project funded by the Texas Water Development Board's Economically Distressed Areas Program (EDAP).[50]

The *Colonia Self-Help Centers Fund* is part of TDRA's TxCDBG program, but is administered by TDHCA through an interagency agreement. The fund assists low-income individuals and families in financing, refinancing, building, improving or maintaining a safe, suitable home in a designated *colonia* service area in a county designated as economically distressed under the EDAP and eligible to receive EDAP funds; the colonias served by the center must be located within 150 miles of the Texas-Mexico border. The TxCDBG program funds the colonia self-help centers.[51]

TDRA also offers a separate *Colonia Planning Fund* to eligible counties located within 150 miles of the Texas-Mexico border. Similar to the Planning and Capacity Building

Fund, this fund also provides assistance for planning activities that assess local needs, develop strategies to address local needs and build or improve local capacity.

Another part of the TxCDBG program, the *Disaster Relief/Urgent Need Funds*, help communities recover from natural disasters, drought, flooding or tornadoes when the governor has proclaimed a state disaster or a federal disaster declaration has been issued. These funds are used to restore basic housing, water and sewer facilities. Priorities for renewable energy projects include public facilities that meet basic human needs such as water and wastewater service. Projects funded must benefit a target area in which at least 51 percent of the residents have low- to moderate-incomes. Projects also may qualify under national objective alternatives defined by HUD. Available funding ranges from $50,000 to $500,000 per project.[52]

TDRA approves financial support for disaster relief and urgent needs if the situation addressed by the applicant was of recent origin, unanticipated and beyond its control. For disaster relief assistance, this means the application for assistance must be provided within 12 months from the date of a presidential or gubernatorial disaster declaration. For urgent-need assistance, the situation must have first occurred or been discovered no more than 30 days prior to the date of a written request to TDRA. The applicant must demonstrate that local funds or funds from federal sources or another state source are not available to address the problem. The TxCDBG program coordinates distribution of funds with other state agencies.

Pilot Program: Renewable Energy Demonstration

In 2007, TDRA developed a renewable energy pilot program, to be funded solely through de-obligated funds and/or program income for demonstration projects that employ renewable energy to meet at least 20 percent of the total energy requirements to power public projects including wastewater treatment or water treatment facilities.

The priority is for renewable energy projects that provide public facilities to meet basic human needs such as water and wastewater service. Projects funded have to benefit a "target area" where at least 51 percent of the residents have low to moderate incomes, although the project would be allowed to qualify under national objective alternatives defined by HUD. Available funding ranges from $50,000 to $500,000 per project.[53]

TDRA designated up to $500,000 in 2009 Community Development Block Grant funds to help eligible rural communities install their own renewable energy projects. Examples of eligible projects could include installing wind turbines or solar panels to power wastewater treatment or water treatment facilities.[54]

TDRA Disaster Recovery Program

Hurricanes Ike and Dolly Funding

In 2008, the Governor's office established TDRA as the lead Texas state agency responsible to the U.S. Department of Housing and Urban Development for grant administration of all TxCDBG disaster recovery funding on behalf of the State of Texas. In this capacity, TDRA is responsible for overseeing the administration of CDBG funds for all housing, non-housing, and economic development disaster recovery activities. In cooperation with TDRA, the Texas Department of Housing and Community Affairs (TDHCA) is responsible for housing recovery related activities.

With the designation as lead agency for all TxCDBG disaster recovery funding and the urgency to allocate funds to affected communities quickly, TDRA established the Disaster Recovery Division dedicated to overseeing the Hurricane Ike/Dolly funding and managing the Hurricane Rita non-housing funds.

Ike/Dolly Round 1 Funding

On Feb. 13, 2009, HUD announced an initial allocation to Texas of $1,314,990,193 under title IV of the Robert T. Stafford Disaster Relief and Emergency Assistance Act due to natural disasters in 2008.[55] A second allocation of $1,743,001,247 was announced Aug. 14, 2009.

Approximately $591,232,327 was allocated to non-housing and economic development that TDRA will oversee. The remaining funds were allocated to TDHCA for housing and administration with project delivery support by TDRA and TDHCA. The initial Action Plan distributed funds to affected regions based upon the FEMA public assistance and individual assistance data available as of Dec. 1, 2008. Responsibility for further distribution of funds was assigned to the regional Councils of Governments, utilizing their objective method of distribution (MOD), with the intent that local officials could best determine local needs. Replicable and verifiable data was required for this process and use of physical damage criteria was strongly recommended. TDRA began receiving application in May 2009. As of Oct. 30, 2009, TDRA had received 220 applications and had awarded $270,611,460.[56]

In cooperation with TDRA, the Texas Department of Housing and Community Affairs (TDHCA) is responsible for housing recovery related activities.

The initial Disaster Recovery Action Plan Round 1 allocations were based on incomplete data with the best information available at that time. Future allocations will use additional data as they become available. For Round 2 funding, TDRA developed a model employing storm impacts and low- to moderate-income population counts to establish a proportional distribution of all funds across the declared disaster area. This distribution was applied to the cumulative total of funds made available by HUD.

Eligible counties include Anderson, Angelina, Aransas, Austin, Bowie, Brazoria, Brooks, Burleson, Calhoun, Cameron, Cass, Chambers, Cherokee, Fort Bend, Galveston, Gregg, Grimes, Hardin, Harris, Harrison, Hidalgo, Houston, Jasper, Jefferson, Jim Hogg, Jim Wells, Kleberg, Leon, Liberty, Madison, Marion, Matagorda, Milam, Montgomery, Morris, Nacogdoches, Newton, Nueces, Orange, Panola, Polk, Refugio, Robertson, Rusk, Sabine, San Augustine, San Patricio, Shelby, Smith, Starr, Trinity, Tyler, Upshur, Victoria, Walker, Waller, Washington, Wharton and Willacy.

Eligible local governments include the Ark-Tex Council of Governments, Brazos Valley Council of Governments, Central Texas Council of Governments, Coastal Bend Council of Governments, Deep East Texas Council of Governments, East Texas Council of Governments, Golden Crescent Regional Planning Commission, Houston-Galveston Area Council, Lower Rio Grande Valley Development Council, South Texas Development Council and the Southeast Texas Regional Planning Commission.

Ike/Dolly Round 2 Funding

In preparation for Round 2 funding and the Sept. 30 deadline for Texas to submit the Action Plan Amendment 1 to HUD, TDRA and TDHCA began a review of the initial action plan, working with the regional and local governments to improve the allocation process and address some concerns related to Round 1 allocations. A series of public meetings were held prior to finalizing the amended Action Plan. The amended Action Plan includes a funding distribution model which includes factors that consider surge, wind and rainfall and low- to moderate-income populations. On Aug. 14, 2009, HUD announced the second allocation of $1,743,001,247. The amended Action

Plan proposes an equal allocation between housing and non-housing activities. The amended plan was submitted to HUD on Sept. 30, 2009, for review and approval. It is anticipated that TDRA will begin accepting grant applications for Round 2 Ike/Dolly funding during the spring of 2010 with funding awards starting in summer 2010 for the non-housing portion of the funds.

Hurricanes Katrina and Rita

In response to hurricanes Katrina and Rita, Texas received two rounds of funding for a total of $116,523,000. TDRA was allocated $73,837,574 for non-housing grants. TDHCA is responsible for the administration of the remaining funds for housing activities. These funds were intended to assist with long-term recovery efforts and infrastructure restoration to restore critical infrastructure available to affected governments located within the four Council of Governments areas (COG) comprised of the following: East Texas Council of Government (ETCOG), Deep East Texas Council of Government (DETCOG), Southeast Texas Regional Planning Commission (SETRPC) and the Houston-Galveston Area Council (HGAC). A total of 102 awards were made possible by the Rita 1 and Rita 2 funding to various local governments. As of October 2009, approximately $28,779,644 or 94.2 percent of the $30,537,574 Rita 1 funding and approximately $21,281,950 or 49 percent of the $42,000,000 Rita 2 funding had been spent. The remainder will be paid upon completion of Rita 1 and Rita 2 projects.

American Recovery and Reinvestment Act and TDRA

The American Recovery and Reinvestment Act (ARRA) appropriated $1 billion to the U.S. Department of Housing and Urban Development's CDBG program to provide funds to states and local governments for eligible activities under the CDBG program. TDRA received about $19.5 million in Recovery Act funds.[57] TDRA was able to fund an additional 75 rural communities and counties that had submitted applications to TDRA for the TxCDBG's Community Development Fund.

Texas State Office of Rural Health

TDRA's Texas State Office of Rural Health programs serve 150 rural hospitals and benefit more than 3 million rural Texans. Its mission is to facilitate and coordinate the use of available resources to help rural Texans enhance their quality of life, achieve sustained economic growth and strengthen local healthcare systems and infrastructure. The office works with local, state and federal partners to develop, support and coordinate programs and services to improve rural access to health services. It also facilitates and guides efforts in rural health policy design, service planning, resource allocation and program implementation.

Community Reinvestment and State Agency Programs

Banking

The Texas Department of Banking (DOB) promotes and supports bank participation in community reinvestment programs. As an incentive for participation, DOB waives corporate fees for applicants that plan to serve low- to moderate-income areas.

Over the years, mergers and acquisitions have reduced the state's number of banks and thrift institution charters, which fell by 20 percent from 1998 to 2008, from 879 to 704. This activity has not decreased the number of branches in Texas, however. Between 1998 and 2008, the number of branch offices in Texas rose by 52 percent.

Due to a relatively healthy state economy, Texas remains attractive to out-of-state financial institutions seeking to expand or relocate. This is reflected in the increasing number of out-of-state banks and thrifts, both state- and nationally chartered, operating in Texas during the last five years. Their number rose by almost 59 percent, from 34 institutions as of June 30, 2003 to 54 as of June 30, 2008.

As of June 2008, the median-sized financial institution operating in Texas controlled about $688 million in deposits. The expansion of the Texas economy, primarily due to surging oil and gas prices, the growth of existing business enterprises and the continuous relocation of businesses to Texas, were the primary causes for continued growth in Texas banking throughout 2007 and early 2008.[58]

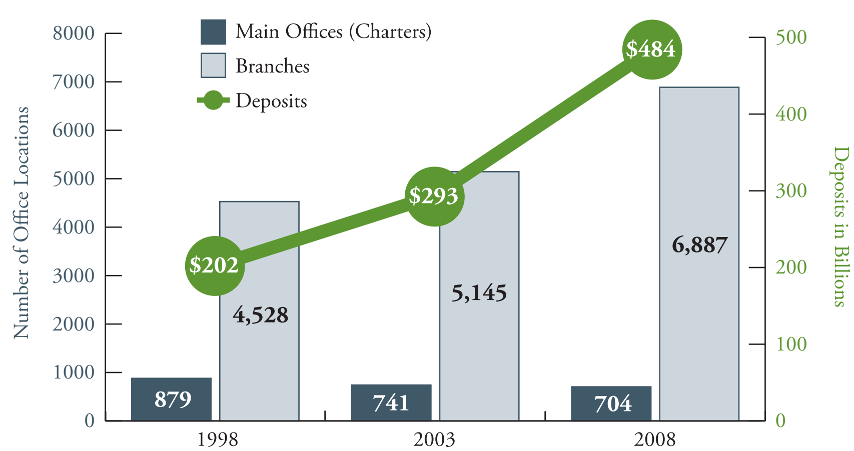

Chart includes branches of banks and savings institutions charted by both national and state authorities, and institutions headquartered either in Texas or in other states. It does not include share value of credit unions operating in Texas. Information is as of June 30 of each year.

Source: FDIC.

Many Texas bankers charged with leading their banks through the current economic slump had previously weathered turbulence and adversity in the 1980s. From past experiences, many seasoned bankers resolved not to waver from safe and sound banking principles. The trend of mergers and acquisitions in the industry continues, however, and is most pronounced among the larger multi-state institutions.

Today's economy is crippled by a different set of problems, including subprime lending, investments in subprime mortgage-backed securities and collateralized mortgage obligations, off-balance sheet derivative activities and credit default swaps. Texas banks in general, particularly community banks, did not participate in many of the activities that are creating financial difficulties in other states. Similarly, Texas residential real estate prices never escalated to the extremes seen in other regions of the country, and did not suffer from the subsequent bubble effects. Through the present economic downturn, Texas continues to benefit from a strong and diversified economy that has helped insulate it from more severe market corrections.

DOB continues to promote financial literacy throughout the state, holding workshops and visiting banks to discuss the benefits of financial education programs. DOB trainers can provide tools and program startup materials for educational programs. Consumer assistance is offered to citizens via several avenues, including the agency Web site's consumer complaint section and agency publications. The agency also continues to review FDIC and CRA examination results for its regulated entities and provides follow-up to ensure that any weaknesses are corrected.

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Economic Development

The Governor's Texas Economic Development and Tourism (EDT) Division maintains an Economic Development Bank created by combining finance programs previously administered by the Texas Department of Economic Development. These programs include the Texas Small Business Industrial Development Corporation, the Industrial Revenue Bond Program established under the Development Corporation Act of 1979 (Article 5190.6, Vernon's Texas Civil Statutes), the Texas Enterprise Fund, the Product Development Fund and the Small Business Incubator Fund established under Government Code, Chapter 489, Subchapter D.

EDT works with companies seeking to expand or relocate into Texas communities and administers programs that encourage the financing of local economic development projects.

The Texas Small Business Fund is a revolving loan program funded with capital from $20 million in taxable bonds issued in 2005. The Economic Development Bank administers the fund at the direction of a governor-appointed board. The fund provides financing to foster and stimulate the development of small businesses in Texas. Preference is given to emerging technology fields including semiconductors, nanotechnology, biotechnology and biomedicine, renewable energy and aerospace, as well as small businesses that have received financing from the state's Small Business Development Centers or through the Small Business Innovative Research program.

EDT has another small-business financing tool in its Product Development Fund, which aids in the development, production and commercialization of new or improved products in Texas. These can include inventions, devices, techniques or processes that are ready for immediate commercial application.

Preference for funding is given to emerging technology fields including semiconductors, nanotechnology, biotechnology and biomedicine, renewable energy and aerospace.

Job creation and job retention within Texas are also priorities. The fund is a revolving loan program with capital provided from $25 million in taxable bonds issued in 2005. The Economic Development Bank administers the fund at the direction of a governor-appointed board.[59]

EDT's Small Business Assistance Section serves as a principal contact point for assistance to small and historically underutilized businesses. The program advocates for small business issues affecting the state.

Housing

The creation of safe and sanitary housing is an obvious requirement for economic development. The Texas Department of Housing and Community Affairs provides a range of housing support programs, from homeless support to disaster recovery.[60]

TDHCA administered $474 million in such funding in fiscal 2008.[61] More than 99 percent of it came from federal sources such as grants and tax credits. It should be noted that, with the exception of the Section 8 Housing Choice Voucher Program, TDHCA administers its programs and services through a network of organizations across Texas and does not fund individuals directly. About 99 percent of the households served by TDHCA housing programs in fiscal 2007 and 2008 had income at or below 80 percent of the area median family income.[62]

Beyond providing for people's basic needs, TDHCA's housing programs also help fuel the Texas economy. The National Association of Homebuilders reports that building an average new single-family home in the U.S. generates 3.05 jobs and $89,216 in government revenue, including construction-related fees imposed by local governments.[63]

Homelessness and Poverty-Prevention Services

For Texans who are homeless or are facing the prospect, TDHCA offers the *Emergency Shelter Grant Program* (ESGP), which funds organizations that renovate buildings for use as shelters or that provide homelessness prevention services. TDHCA committed more than $4.7 million to the program in fiscal 2008, indirectly serving 111,291 individuals.[64]

The American Recovery and Reinvestment Act of 2009 (ARRA) created a new program called the *Homelessness Prevention and Rapid Re-Housing Program* (HPRP) to help prevent homelessness. TDHCA was allocated about $41.4 million from HPRP, awarding it to local units of government and qualifying nonprofit organizations. The funds are to be used for homelessness prevention assistance and to rapidly re-house persons who are homeless. TDHCA must spend 100 percent of the funds within three years of July 2009.[65]

For Texans struggling to pay costs associated with their housing, TDHCA offers the *Comprehensive Energy Assistance Program* (CEAP), which funds organizations that provide utility assistance to households with an income at or below 125 percent of federal poverty guidelines. Some low-income households can qualify for the repair, replacement or retrofitting of inefficient heating and cooling appliances through CEAP. CEAP committed more than $46.9 million in fiscal 2008 to serve 68,055 households.

To further assist lower-income persons in retaining their housing, TDHCA provides administrative funds through the *Community Services Block Grant* (CSBG) program to community action agencies (CAAs) that may be part of units of local government or stand-alone nonprofit entities. CAAs offer services that can be essential to preventing homelessness, such as child care, health and human services, job training, farm worker assistance, nutrition services and emergency assistance. In fiscal 2008, TDHCA committed almost $28.8 million in CSBG program funds to serve 500,296 individuals. Through ARRA, TDHCA made an additional $48.1 million in funds available for the CSBG. Services performed due to these funds must be provided by Sept. 30, 2010.[66]

The 81st Texas Legislature appropriated $20 million in general revenue funds over the fiscal 2010-11 biennium for the *Homeless Housing and Services Program* (HHSP), which TDHCA will administer. The funds will be used to assist regional urban areas in providing services to homeless individuals and families. Funds will cover case management, construction of facilities, direct services, homeless prevention, housing retention and rental assistance. TDHCA will award funds through a competitive matching grant process. Eight of the state's largest cities will seek additional funding to meet the grant's matching fund requirement. Applications for HHSP became available in October 2009.[67]

Under HHSP, TDHCA will provide financial assistance to political subdivisions, housing finance corporations, for-profit corporations and nonprofit organizations to support local initiatives for homeless individuals and families. TDHCA also will seek federal funding to provide financial assistance under HHSP.

The 81st Texas Legislature appropriated $20 million in general revenue funds over the fiscal 2010-2011 biennium for the Homeless Housing and Services Program (HHSP), which TDHCA will administer. The funds will be used to assist regional urban areas in providing services to homeless individuals and families.

Rental Assistance

TDHCA offers a wide range of rental assistance, from subsidized rents to subsidizing developments that offer reduced rent for low-income Texans.

The *Section 8 Housing Choice Voucher Program* provides rental assistance payments on behalf of low-income households whose incomes do not exceed 50 percent of federal median income guidelines. The federal government requires that 75 percent of all new households admitted to the program be at or below 30 percent of the AMFI. Qualified households may select housing through direct negotiations with landlords and TDHCA will pay approved rent subsidies directly to the property owners. In fiscal 2008, TDHCA committed $5.8 million for the program, serving 1,109 households.

The *HOME Investment Partnerships Program* offers grants and loans to local governments, nonprofit agencies, for-profit entities and public housing agencies that provide safe, decent and affordable housing to low-income families. HOME has a 15 percent set-aside for community housing development organizations and a 5 percent set-aside for people with disabilities. The program offers both a Tenant-Based Rental Assistance Program that subsidizes rent for low-income Texans as well as a Rental Housing Development and Rental Housing Preservation Program that assists the development of housing for eligible households.

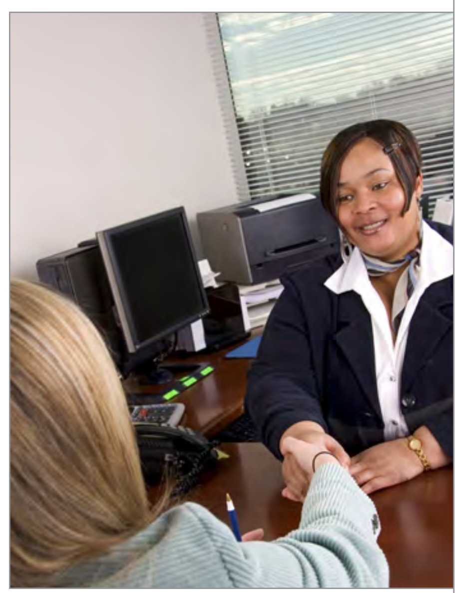
In fiscal 2008, TDHCA committed more than $4.1 million for Tenant-Based Rental Assistance, more than $17.7 million for new rental construction and more than $8.1 million for rehabilitation of rental units. TDHCA served a total of 919 households in fiscal 2008 with HOME rental assistance funds.

The *Housing Trust Fund* is a state-authorized program dedicated to increasing the state's supply of affordable housing. The program's funds are legislatively authorized and competitively awarded by TDHCA for rental assistance as well as the acquisition, rehabilitation and new construction of affordable rental housing or homeowner developments. In fiscal 2008, TDHCA committed more than $812, 000 in rental assistance for 86 households.

TDHCA's *Multifamily Mortgage Revenue Bond Program* issues mortgage revenue bonds to finance loans for qualified nonprofit organizations and for-profit developers that create low-income rental housing. Financed properties assist low-income households and must meet "unit set-aside restrictions" that may include rent limitations and other requirements set by TDHCA.

Project developers may elect to set aside 20 percent of the units for households earning 50 percent or less of the AMFI, or 40 percent of the units for households earning 60 percent or less of the AMFI. In fiscal 2008, nearly $41.1 million was committed for new construction of rental units serving 672 households.

The *Housing Tax Credit Program* provides a tax credit for developers of low-income rental housing to offset a portion of their federal tax liability in exchange for building affordable rental housing. To qualify for the tax credit, 20 percent or more of a project's units must be rent-restricted and occupied by individuals whose income is 50 percent or less of the AMFI; or 40 percent or more of the units must be rent-restricted and occupied by individuals whose income is 60 percent or less of the AMFI. TDHCA committed more than $38.8 million from the Housing Tax Credit Program in fiscal 2008 for new rental units to serve 3,803 households, and another $13.8 million for the rehabilitation of rental units for 2,128 households.[68]



The *Tax Credit Exchange Program*, a new federal program created by the ARRA, allows developments that have received Housing Tax Credits in fiscal 2007 and 2008 through September 2009 to exchange their credits for a cash grant. In October 2009, TDHCA applied for funding under this program of up to $314 million. TDHCA must return any unused funds by January 2011.

The ARRA also created a new program under the HOME Investment Partnerships Program, the *Tax Credit Assistance Program*. This provides funds to offset the current devaluation of Housing Tax Credits. The economic recession of 2008 and 2009 decreased investor demand for these credits, causing their price to fall and jeopardizing the financial stability of affordable rental developments previously awarded Housing Tax Credits. The Tax Credit Assistance Program seeks to address the lost value of these credits by allowing TDHCA to award HOME funds to developments affected by the devaluation. About $148 million is available for this program and property owners receiving these awards must expend them by February 2012.[69]

Homebuyer Assistance

After a low-income household becomes self-sufficient, it may be ready for homeownership. TDHCA makes efforts to ensure that potential homeowners understand the responsibilities involved by offering homeownership education courses and training, as well as financial tools to help smooth the transition to homeownership.

Adequate homebuyer counseling may reduce mortgage delinquency and foreclosure rates. To ensure that lenders, borrowers and policymakers understand the full scope of TDHCA lending programs, TDHCA created the *Texas Statewide Homebuyer Education Program (TSHEP)* in 1999. TSHEP provides homebuyer counseling through experienced education providers, nonprofit housing providers, low-income housing advocates, for-profit housing providers, lenders and realtors. As of October 2009, TDHCA has trained and certified 580 individuals.[70]

TDHCA also offers financial tools to help households purchase homes. The *Single-Family Bond Program* raises funds through tax-exempt and taxable mortgage revenue bonds to finance the *First-Time Homebuyer Program*. The *First-Time Homebuyer Program*, in turn, offers 30-year, below-market, fixed-rate mortgages for households whose incomes do not exceed 115 percent of the AMFI and who qualify as first-time homebuyers. Eligible households must work with participating lenders to secure a loan. Thirty percent of First-Time Homebuyer funds are set aside for households earning 60 percent or less of the program income limits.[71]

The *First-Time Homebuyer Program* works in conjunction with the *Grant Assistance Program (GAP)* and *Mortgage Credit Certificate (MCC)* program. GAP provides up to 5 percent of the loan amount for down payments and closing costs. The funds are available on a first-come, first-served basis for mortgage loans originated through the *First-Time Homebuyer Program*. Assistance is available to eligible borrowers whose incomes do not exceed 80 percent of AMFI. The *MCC* provides tax credits that reduce the federal income taxes, dollar for dollar, of qualified buyers purchasing a qualified residence. The amount of the annual tax credit can cover up to 35 percent of the annual interest paid on a mortgage loan, cannot exceed $2,000 per year and cannot be greater than the household's total annual federal income tax liability. The *MCC* is available for households whose income does not exceed 115 percent of AMFI limitations based on IRS-adjusted income limits.[72]

TDHCA is the lead agency in a partnership for Hurricane Katrina and Rita disaster recovery, with TDRA, the city of Houston, Harris County and Southeast Texas.

More than $233.1 million was committed for the *Texas Single-Family Bond Program* in fiscal 2008. This sum included funds for the *First-Time Homebuyer Program*, the GAP and the *MCC*, which together served 2,065 households.[73]

The ARRA allows for eligible first-time homebuyers to receive a tax refund equal to 10 percent of the purchase price of their home or $8,000, whichever is less. The refund applies to home purchases made between Jan. 1, 2009, and Dec. 1, 2009. In June 2009, TDHCA launched the *90-Day Down Payment Assistance* and *Mortgage Advantage* programs to allow potential homebuyers to take advantage of the federal first-time homebuyers' tax credit for down payment and closing costs.[74]

The *90-Day Down Payment Assistance Program* provides 5 percent of the first lien mortgage amount up to a maximum of $7,000 for down payment and closing costs at no interest for 90 days. The *Mortgage Advantage Program* provides 5 percent of the first lien mortgage amount up to a maximum of $6,000 for down payment and closing costs when combined with the *Texas First Time Homebuyer* or *MCC* Programs. The *Mortgage Advantage Program* offers 0 percent interest on the second lien for 120 days. As of September 2009, TDHCA had received about 700 loan applications under these two programs. Total allocation for the *90-day Down Payment Assistance Program* totaled $5 million for fiscal 2009 and fiscal 2010 and $2.5 million for the *Mortgage Advantage Program*. Mortgage revenue bond funds provided this funding.[75]

To assist low-income households with down-payment and closing costs, *HOME* allocates funds through *Homebuyer Assistance* and *Homebuyer Assistance with Rehabilitation (HBAR)* programs. HBAR funds also may pay for construction costs associated with architectural barrier removal, in a home purchased with HOME assistance, to meet a disabled homebuyer's accessibility needs. TDHCA committed about $4.4 million for these programs in fiscal 2008, serving 448 households.[76]

TDHCA's *Contract for Deed (CFD) Conversion Initiative* helps residents of colonias become property owners by converting their CFDs into traditional mortgages. In fiscal 2007, $2 million was dedicated to CFD Conversions; $2 million was dedicated to CFD conversions in fiscal 2008.[77]

The Bootstrap *Homebuilder Loan Program* is a statewide loan program offered through certified nonprofit organizations to allow owner-builders to purchase real estate to construct or renovate a home. Two-thirds of these funds must be committed in economically distressed areas, as defined by the Texas Water Development Board. Participating owner-builders must provide a minimum of 60 percent of the labor required to build or rehabilitate the home. Total loans from TDHCA cannot exceed $30,000 per unit. The Bootstrap program is funded through the Housing Trust Fund. More than $5.4 million was committed to the program in fiscal 2008.[78]

Weatherization and Rehabilitation Assistance

Low-income homeowners may need weatherization services to help them control energy costs and keep their homes affordable. They also may need more substantial rehabilitation or reconstruction. To meet these needs, TDHCA funds a network of organizations that provide weatherization and rehabilitation for low-income homeowners.

TDHCA offers the *Weatherization Assistance Program (WAP)*, which helps households control their energy costs by installing storm windows, attic and wall insulation and weather-stripping and sealing. It also provides energy conservation education. Assistance is prioritized for the elderly, persons with disabilities, families with young children, households with the highest energy costs in relation to income and households with high-energy consumption. TDHCA committed more than $12.2 million for WAP, serving 3,941 households in fiscal 2008. From the ARRA, TDHCA received more than $326.9 million in additional funding for WAP that must be expended by March 2012.

The *HOME Investment Partnerships Program* also allocates funds through an *Owner-Occupied (OCC) Housing Assistance Program* to provide repair or reconstruction of low-income homeowners' existing homes, which must be their principal residences. At the completion of the assistance, all properties must meet the Texas Minimum Construction Standards, the International Residential Code and local building codes. More than $4.3 million was committed in fiscal 2008 for rehabilitation services for 97 households.[79]

The *Housing Trust Fund* also provides funds for rehabilitation of single-family homes. TDHCA committed $338,137 from this source to single-family home rehabilitation activities in fiscal 2007. In fiscal 2008, TDHCA committed more than $1.9 million in *Housing Trust Fund* money to single-family home rehabilitation activities that served 127 households.[80]

Disaster Recovery and Relief

Low-income homeowners and renters often are the most severely affected and the last to recover when natural disasters strike.[81] In 2005, a large number of evacuees from Louisiana escaped to Texas during Hurricane Katrina; shortly afterward, more than 75,000 homes in Southeast Texas were severely damaged by Hurricane Rita. TDHCA offers disaster recovery programs to address the essential needs of persons displaced by natural disasters, to speed community recovery.

TDHCA is the lead agency in a partnership for Hurricane Katrina and Rita disaster recovery, with TDRA, the city of Houston, Harris County and Southeast Texas. TDHCA's Disaster Recovery Division works within this partnership to administer two federal community development block grants.[82] Texas received $74.5 million under

Public Law 109-148 in May 2006 and an additional $428 million under Public Law 109-234 for recovery efforts in Southeast Texas.[83] By August 2007, housing-related activities had accounted for $853,698 and non-housing-related activities had used $4.5 million. By October 2009, housing-related activities accounted for $138.7 million and non-housing activities had used more than $18.8 million.[84]

TDHCA's Community Services Division reserves a portion of the state's Community Services Block Grant (CSBG) funds for low-income persons at 125 percent and below of the federal poverty income guidelines that live in communities affected by disaster. The CSBG emergency disaster relief funds provide persons with emergency shelter, food, clothing, pharmaceutical supplies, bedding, cleaning supplies, personal hygiene items and essential appliances including stoves, refrigerators and water heaters. A total of $885,000 in CSBG funding was awarded in fiscal 2008 for disaster-related activities.

Many homeowners look to TDHCA for recovery aid when they have no other means of assistance or when they need gap financing after receiving federal assistance. To meet these needs, TDHCA may use deobligated HOME funds for disaster relief awards through HOME's OCC *Housing Assistance Program*. HOME disaster funds help eligible homeowners pay for the repair, rehabilitation and reconstruction of existing homes affected by disaster. They must live in the home as their primary residence and must be at or under 80 percent of AMFI. About $3 million in HOME funds were used for disaster recovery in 2008.

Many regular insurance companies have ceased writing risks in these coastal areas due to concerns about hurricanes.

Because the Housing Trust Fund is not restricted by federal guidelines, it can also be used for disaster recovery. TDHCA approved the use of $1.2 million from the Housing Trust Fund in 2008 for a *Disaster Recovery Homeowner Repair Gap Financing Program* to aid homeowners affected by Hurricane Rita. The program was created to assist qualified households who lacked only a small portion of the funds needed to meet the full cost of construction and repairs.[85]

To further reinforce hurricane recovery efforts, TDHCA's *Single-Family Bond Program* announced the release of $15.6 million in June 2007 for home loans to qualified homebuyers wishing to purchase within the 22 East Texas counties designated under the Gulf Opportunity Zone Act. This federal act established tax incentives and bond provisions to support rebuilding in areas devastated by the hurricanes of 2005. In September 2007, TDHCA released an additional $32 million through the First-Time Homebuyer Program, which is funded through the Single-Family Bond Program, for use within targeted areas including the 22-county area known as the Rita Go Zone.[86]

Housing Programs Fiscal 2008

Program	Amount Committed Fiscal in 2008
Emergency Shelter Grant Program	$4.7 million
Comprehensive Energy Assistance Program	$46.9 million
Community Service Block Grant Program	$28.8 million
Section 8 Housing Choice Voucher Program	$5.8 million
HOME Investment Partnerships Program (all activities)	$38.8 million
Multifamily Mortgage Revenue Bond Program (all activities)	$41.1 million
Housing Tax Credit Program (all activities)	$52.7 million
Single-Family Bond (all activities)	$233.1 million
Housing Trust Fund (all activities)	$9.8 million

Housing Programs Fiscal 2008 (cont.)

Program	Amount Committed Fiscal in 2008
Contract for Deed Conversion Initiative**	$2.0 million
Texas Bootstrap Loan Program	$5.4 million
Weatherization Assistance Program	$12.2 million

**Does not include disaster-related funds.*
***Amount dedicated to this program.*
Source: Texas Department of Housing and Community Affairs.

Insurance

The Texas Department of Insurance regulates the Texas insurance market, which includes more than 1,900 insurance companies, health maintenance organizations and other insurance risk-bearing carriers. TDI's functions include regulating the financial solvency of insurance companies, regulating policies and rates and providing consumer protection services.

TDI prepares a biennial report on investments made in Texas by life and health insurance companies with $10 million or more in Texas premiums. A total of 280 companies met these criteria and accounted for about 98 percent of the total life and annuity premiums collected in Texas in calendar 2007.

TDI's biennial report for 2008 identified $43 billion in Texas investments made by these insurers. Ninety-five percent of their reported investments were in commercial and farm mortgages, political subdivision/public utility bonds and corporate bonds. The largest amounts by category were commercial and farm mortgages ($17.3 billion), political subdivision/public utility bonds ($12.4 billion) and corporate bonds ($10.3 billion).

These amounts, however, are not comprehensive, since many of the reporting companies cannot link their investments to an individual state. This is also the case with pooled investments.

Insurance company residential mortgage investments are frequently made through pooled investments; comprehensive data are not available for this category. Due to the difficulty involved in linking some corporate bond investments to specific states, reporting for that category is optional. Furthermore, Texas investments made by property and casualty insurance companies are not included in the above amounts because they are not subject to the statute requiring these reports. Additional information about these investments can be found in the *December 2008 Community Investment Report* available on the TDI Web site at www.tdi.state.tx.us.

TDI attempts to ensure that property insurance remains available and affordable in the state since it is a key to homeownership for millions of Texans. Homeowner's insurance is required on properties that carry liens, so a shortage of available insurance can directly affect a person's ability to purchase a property.

These concerns led to the implementation of the state's Fair Access to Insurance Requirements (FAIR) Plan. The Texas FAIR Plan Association (TFPA) is an entity established by Texas Insurance Code Chapter 2211, Article 21.49A to provide residential property insurance to qualified Texas citizens who find it difficult to obtain coverage from licensed insurance companies. This alternative market is a residual market of last resort and is not intended to compete with the standard property insurance market.

Consumers who have been declined residential property insurance by at least two insurance companies in Texas may apply for coverage. Limited coverage is available for one- and two-family dwellings, townhouse units and condominium units that are owner-occupied, as well as for rental dwellings (one- and two-family) and their contents, and the personal property of tenants living in rental dwellings or apartments. As of April 30, 2008, TFPA had approximately 91,400 policies in force, generating close to $71.9 million in annual premiums.

Another residual market, the Texas Windstorm Insurance Association (TWIA), provides wind and hail coverage in 14 Texas coastal counties and certain portions of Harris County that are exposed to losses from hurricanes. Many regular insurance companies have ceased writing risks in these coastal areas due to concerns about hurricanes. TWIA provided about $65 billion in coverage as of March 31, 2008.[87]

Certified Capital Company State Economic Development

A CAPCO is an investment vehicle, created by experienced venture capital investment managers, in the form of a Limited Liability Corporation or Partnership. Texas law requires CAPCOs to invest 30 percent of their capital in "strategically located" businesses and 50 percent in "early-stage" businesses within five years of receiving funding.

The Comptroller's office and the Texas Treasury Safekeeping Trust Company administer the $400 million Texas Certified Capital Company (CAPCO) program. Funded by insurance premium tax credits, the CAPCO program supports economic development and generates tax revenues for the state by encouraging business growth and job creation. Insurance companies operating in Texas must pay a state tax based on a percentage of the premiums they collect from businesses and individuals. The tax ranges from 1.0 to 1.5 percent. Insurance companies that invest in a CAPCO may claim their investment, dollar for dollar, as a reduction or credit against the taxes they owe.

A CAPCO is an investment vehicle, created by experienced venture capital investment managers, in the form of a Limited Liability Corporation or Partnership. During 2005, ten Texas CAPCOs were certified to raise $200 million through the issuance of certified capital notes or "qualified debt instruments" to insurance companies (Program I). In return for their investments, 110 participating insurance companies will receive premium tax credits equal to 100 percent of the amount of their investments. During 2007, a second round of premium tax credits was authorized in the amount of $200 million (Program II). Investments made under Program II began during calendar 2008.

Texas law requires CAPCOs to invest 30 percent of their capital in "strategically located" businesses and 50 percent in "early-stage" businesses within five years of receiving funding. Based on investment commitments from eligible insurance companies (those with premium tax liabilities to the state), each CAPCO requested an allocation from the total $400 million in available premium tax credits.

For Program I, the tax credits may not be used until 2009 and are restricted to offsetting future insurance premium taxes. Credits may be used, starting with the 2008 return, at a maximum rate of 25 percent of earned insurance premium tax credits annually. Credits for Program II may be used, starting with the 2013 return, at a maximum rate of 25 percent of earned insurance premium tax credits annually.

CAPCOs repay the insurance company investors over time with a combination of earnings on their investments and future tax credits. CAPCOs earn the tax credits by investing in targeted businesses. A CAPCO must meet certain investment criteria and timeframe milestones, pay annual certification renewal fees to the Comptroller's office and adhere to reporting and spending requirements.

CAPCOs may ask the Comptroller's office to determine whether their investments are considered "qualified business investments" under the program rules. The Comptroller's office must review the request and make a determination within a short time frame or the business investment becomes automatically qualified. The Comptroller's office reviews each CAPCO annually to ensure compliance with program requirements. Each CAPCO submits annual reports to the Comptroller's office with a nonrefundable fee of $5,000.[88]

By Dec. 15 of each biennium, the Comptroller's office must report CAPCO-related job creation and program data to the governor, lieutenant governor, and speaker of the Texas House of Representatives. The Comptroller's office publishes the *Certified Capital Companies in Texas Report* on Dec. 15 of each even-numbered year.

Community Development Corporations in Texas

Financial institutions comply with CRA requirements by making loans to low- and moderate-income borrowers for homes, home-improvement projects and small-business ventures. Banks and savings and loans receive favorable credit toward CRA examination ratings by extending loans to and making investments in community development corporations.

CDCs provide affordable housing loans for low-income borrowers, manage loan funds for housing development and help residents plan and track new investments in safe, sanitary and affordable housing and home reconstruction to meet local building codes in low-income rural areas. These organizations also find and evaluate home financing and deliver financial literacy education, tenant counseling, senior citizen programs and community organizing activities to Texas communities in need.

A cumulative total of 259 CDCs and community development financial institutions responded to the Texas Association of Community Development Corporations' (TACDC's) Accomplishments Survey in 2000, 2002, 2004 and 2006. Respondents reported providing more than $216 million in loans to community businesses and residents statewide through 2005.

Of the 259 survey respondents, 210 reported producing affordable housing or actively planning to do so in 2006 and 2007. Thirty-nine organizations completed or planned to complete commercial or industrial projects including office space, commercial kitchens and a medical complex, while 25 CDFIs provided housing or business loans through 2005 or planned to do so in 2006 and 2007. TACDC plans to conduct a new survey of CDCs and CDFIs in late 2009 to assess their accomplishments since 2006.

CDCs in the 2006 survey indicated that they had built 53,045 affordable housing units through 2005. This housing included units built in five principal Texas metropolitan areas — Dallas, Houston, San Antonio, Fort Worth-Arlington and Austin-Round Rock — and along the Texas-Mexico border. The CDCs planned to construct an additional 5,089 units in 2006 and 2007. Of units built in 2004 and 2005, 65 percent were available to those earning between 31 percent and 80 percent of the average median family income, while about 32 percent were offered to households earning less than 30 percent of the AMFI.[89]

Community Reinvestment Issues and Initiatives

Financial Literacy in Texas: Surveys, Legislation, Private and Public-Sector Efforts

How does Texas rank in personal financial literacy? Since the 2007 update, a university research survey examined the basic financial literacy knowledge of Texans and produced some interesting results.

A statewide survey of Texas residents conducted in fall 2008 by Texas Tech's Earl Survey Research Lab found that only one in four respondents was financially "literate." Most had difficulty answering basic questions about adjustable-rate mortgages, employee benefits, insurance deductibles, investments and retirement.

The "Financial Literacy Assessment Survey," administered to 502 residents across Texas by telephone interview, included 26 questions. According to Texas Tech researchers, an estimated 25 percent of those interviewed thought that the FDIC or the SEC guard investors against stock market losses. Sandra Huston, survey coordinator and associate professor at Texas Tech, concluded that many Texas residents do not have the tools needed to make basic financial decisions. The survey also found that:

- many Texans have a limited understanding of credit and insurance. For example, they do not understand that an adjustable-rate mortgage allows the borrower to obtain higher loan amounts.
- survey scores increased with the age of respondents, up to 65 years old, and decreased for the state's oldest and youngest residents.
- Dallas and Houston ranked as the state's most financially literate regions, while the least-literate areas were in East and Northwestern Texas.[90]

Texas' financial literacy education efforts began with the 79th Legislature's House Bill 492, which added Texas Education Code, 28.0021 to require the State Board of Education (SBOE) to review and approve materials for use in teaching personal financial literacy in economics courses. SBOE approved and recommended these materials in June 2009. School districts must use these materials in personal financial literacy courses that are used for an economics credit.

Nationally, the Jump$tart Coalition for Personal Financial Literacy reported that a 2008 survey of 6,856 high school seniors in 40 states found many students have difficulties with financial literacy. Out of 31 questions on the survey, students answered only 48.3 percent of them correctly, compared to 52.4 percent for the senior class of 2006, two years earlier. The survey also found that:

- only about 36 percent believed a house with a fixed-rate mortgage is a good way to guard against inflation;
- only 40 percent of students understood that they could lose their health insurance benefits if their parents became unemployed;
- only 27.3 percent of high school students understand that savings account interest is taxable if the account owner's income is high enough;
- 17 percent correctly answered that savings accounts, savings bonds and checking accounts typically yield lower returns than stocks; and
- 48 percent correctly answered that paying the minimum amount due on a credit card balance will result in higher annual finance charges than paying the full balance each month.[91]

How does Texas rank in personal assets and financial literacy?

- Texas has the lowest average credit scores in the U.S. (666 in Texas compared to a national average of 692).[92]
- Texas has the highest rate of delinquent loan payments of any state.[93]
- Texas also leads the states in its volume of payday lending transactions, which are frequently issued as small cash loans secured by a personal check held until the loan is paid.[94]

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Financial Literacy Education and Outreach in Texas

During the past decade, a growing number of analysts, banking professionals, personal finance counselors, policymakers and educators across Texas have become involved in spreading financial literacy.

The Financial Literacy Coalition of Central Texas attracts community volunteers from industry, nonprofits and public agencies. Spanish-speaking volunteers provide education and outreach. Current initiatives include educational programs for first-time homebuyers, the prevention of mortgage loan fraud, Earned Income Tax Credit education and employee financial education.

In 2005, the partnership Texas Saves was launched to provide literacy training. The organization involves banks, community-based organizations, financial services companies, universities (including the Texas A&M Cooperative Extension) and schools. Texas Saves' financial education campaign works in partnership with other groups across the country, including the Consumer Federation of America and the Junior Finance Literacy Academy.

Since 2007, the Texas Cooperative Extension, Texas Credit Union Foundation and the National Endowment for Financial Education (NEFE) have partnered to bring free, accredited high school financial planning programs and training to Texas schools. Financial literacy efforts of credit unions across Texas include the following:

- Amarillo Community Federal Credit Union provides financial literacy education and materials to Amarillo-area nonprofit organizations, student associations and schools. It assisted 400 students between September 2008 and February 2009.

- the Amarillo and Canyon independent school districts use NEFE materials and reported 1,549 seniors from AISD and 264 from CISD successfully finished the required curriculum as of February 2008.
- Randolph Brooks Federal Credit Union in San Antonio collaborated with the Financial Planning Association and San Antonio's CPA Society to teach 200 students financial literacy at 10 San Antonio-area high schools in 2008.
- Texans Credit Union partnered with the Frisco Independent School District to bring the financial literacy curriculum into its classes using the NEFE materials. For the 2007-08 academic year, Texans partnered with Junior Achievement of Dallas to reach 600 students through W.H. Adamson High School in the Frisco ISD, making it the state's first credit union to adopt a high school for financial literacy education.
- Dupont Goodrich Federal Credit Union (DGFCU) established a school/business partnership to open a "Student Financial Center" with an ATM on the campus of West Brook High School in Beaumont. Open since 2004, the center handles more than $150,000 in transactions annually, has opened more than 450 accounts and makes loans. DGFCU also provides money fundamentals education to local Girl Scout troops and 12-week financial management training courses to the Christian Women's Job Corp.[96]

In 2009, the Texas Department of Banking scheduled train-the-trainer financial education workshops in Dallas, Houston and Lubbock, among other cities.

Payday, "Predatory" and Subprime Lending

The economic crisis has revealed a number of weaknesses in the U.S. financial system and brought into tighter focus the impact that payday, "predatory" and subprime lending practices have on the finances of low-income borrowers.

Traditional "prime" home loans from banks, generally made to borrowers with high credit scores, often offer competitive low-interest rates with a minimum of additional charges and loan fees. Other loans carry higher interest rates and fees and usually are made to households that have relatively poor credit scores or lack credit histories altogether.

- *Subprime* home loans and mortgages generally are at least three or four points higher than home loans made in the prime market. The Federal Reserve Board has found that more than half of subprime mortgages have adjustable rates, with an initial period of two to three years of fixed payments followed by variable payments.
- *Payday* lending refers to the practice of making short-term "payday loans," generally as small cash advances based on a personal check held for future deposit. These are often provided by check-cashing outlets, pawnshops, stand-alone companies and online or telephone loan providers. Many payday loans only require disclosure of income from a job or government benefits and a driver's license. Promoted as a way to relieve interruptions in cash flow, payday loans can carry interest rates as high as 400 percent annually.[97] As of January 2009, 41 states and the District of Columbia had payday lending laws.[98]
- *Predatory* lending refers to making loans with excessive fees, hidden loan terms and very high interest rates with little, if any, verification of the borrower's ability to

repay. Most predatory lenders locate in low-income or disadvantaged communities, close to customers that lack good credit and have few assets and unreliable or very low incomes.

Subprime Lending and the CRA

In 2008, FRB analysts examined what, if any, role the CRA played in the subprime mortgage loan crisis. The FRB's study concluded that the CRA was not a contributing factor. Pointing to mortgage purchase data, FRB noted that mortgage payment delinquency rates were high across all neighborhoods, regardless of income. Although low-income households presented the highest 90-day delinquency rates, these homeowners represented only a fifth of delinquent mortgage totals.[99]

The FRB suggested the "originate-to-distribute" subprime loan model provided independent and unregulated lending operations and mortgage brokers with a sizeable window of opportunity to quickly make large profits. Mortgage brokers and subprime mortgage loan originators, operating without federal or state regulatory oversight, used the originate-to-distribute model to sell loans to secondary markets rapidly, with the intention of making fast profits from originating closing fees and commissions on a large quantity of loans. The fact that loans were originated with the intention of quick sell-off to the secondary markets made it less important to evaluate their high risk of nonpayment and failure potential.

As of April 2009, 0.8 homes in Texas were in foreclosure out of every 1,000 housing units. Out of every 1,000 Texas homes financed as of April 2009, almost 53 percent were paid late at least once in the previous 12 months.

To further support its conclusion that the CRA did not cause the subprime crisis, the FRB's analysis compared loans made by banks in CRA-assessment areas in 15 of the largest U.S. metro areas with loans made by other lenders in each market. Banks were found to make fewer high-cost loans to low- and moderate-income borrowers than other lenders. Also, banks in their CRA assessment areas were twice as likely as other lenders to keep the loans they originated.[100]

Subprime Market Foreclosures in the U.S. and Texas

The following factors helped fuel the growth of the Texas subprime loan market:

- broker abuse and incentives that lured unqualified borrowers into unaffordable subprime loans;
- failure to escrow property taxes and hazard insurance;
- "exploding hybrid" high-risk mortgages with low-interest teaser rates;
- lack of action by FRB to address predatory lending actions by mortgage brokers, banks and other entities;
- low- and no-documentation loans with layered risks in a single loan; and
- nonstandard mortgage qualification practices and irresponsible loan underwriting.[101]

The subprime loan market was driven by the easy availability of high-risk loans with low-interest "teaser" rate payments for the first two years. Examples include "exploding" hybrid mortgages, known as "2/28s," with a two-year balloon loan that cannot be repaid in monthly installments, but must be repaid in one lump sum. The "2/28" is an adjustable rate mortgage that starts with a two-year teaser "balloon" rate component and rate adjustments every six months for the rest of the loan term. Generally, the rate of interest climbs by 1.5 to 3 percentage points by the end of the second year.[102]

The U.S. and Texas are watching the most serious foreclosure crisis in America since the Great Depression. Foreclosure filings in 2008 were up 81 percent over 2007. This equates to 3,700 foreclosures each business day for 2008. More than 8 million American homes may face foreclosure in the next four years, according to the National Consumer Law Center, Inc.[103] As of April 2009, 0.8 out of every 1,000 housing units in Texas were in foreclosure. Out of every 1,000 Texas homes financed as of April 2009, almost 53 percent were paid late at least once in the previous 12 months.[104]

Examples of existing state foreclosure laws that may accelerate the loss of homes and wealth include the following:

- except in California and Connecticut, a mortgage holder can push a home to foreclosure directly without any requirement to modify the terms of the loan;
- no U.S. mortgage holders have any legal obligation to halt foreclosure if the homeowner produces the owed payments and incurred penalties and fees;
- except in Massachusetts, New Jersey and Pennsylvania, mortgage holders that claim a homeowner has fallen behind in payments can immediately impose default costs and fees that weaken the chance for the homeowner to catch up on back payments.

While Texas residential loan applicants entered into a comparatively higher number of commercial subprime mortgages than in other parts of the U.S. from mid-2003 through mid-2007, by 2009 Texas ended up with less-severe delinquency and foreclosure problems. Texas has a higher ratio of homeowners' equity in subprime loans and fewer of the riskier adjustable-rate mortgages and cash-out refinancing.

According to a second-quarter 2008 report by the Dallas Federal Reserve Bank, the Dallas-Fort Worth and Houston-Sugar Land metro areas had the most subprime mortgages, followed by San Antonio, Austin-Round Rock, McAllen-Edinburgh-Mission and Corpus Christi. Wichita Falls (20 percent) ranked highest among Texas' smaller metros in subprime delinquency rates, while Odessa (10 percent) had the lowest share.

As of February 2009, 30 states and the District of Columbia allowed "fast-track" foreclosure of homes owned by individuals alleged to have fallen behind on home payments. In 33 states and the District of Columbia, no legal requirement ensures that homeowners are personally served with a foreclosure notice or the legal documents that start a court foreclosure case.[105]

In 2009, the Addison, Texas-based Foreclosure Listing Service, Inc. analyzed 19 metropolitan counties tracked by its service and found that 18 saw a rise in foreclosure postings for April 2009 compared to the same month in 2008. Williamson County experienced the highest increase in house foreclosure postings, with 341 filed in April 2009 compared to 171 in April 2008. Guadalupe County's filings rose by 91 percent, from 34 homes posted in April 2008 to 65 in April 2009. Comal County saw a rise of 79 percent, from 29 notices filed in April 2008 to 52 in April 2009. Bexar County experienced an increase of 65 percent, while Austin's rose by 75 percent. The lowest percentage change in foreclosure postings occurred in Dallas-Fort Worth, up only 27 percent between April 2008 and April 2009.[106]

Agency Strategies to Promote Community Reinvestment in Texas

Each member of the Community Reinvestment Work Group submitted their agency strategies for promoting community reinvestment in Texas in 2009 and 2010. These strategies do not necessarily reflect the views of all members of the Community Reinvestment Work Group.

Banking Strategies

The Texas Department of Banking (DOB) supports financial institutions participating in government-sponsored programs designed to encourage community reinvestment. DOB waives corporate fees for applicants that plan to serve low- to moderate-income areas.

The agency provides consumer services through several channels, including the consumer assistance section of its Web site and agency publications. DOB works to assess how well banks are meeting the needs of their communities by performing follow-up reviews on actions taken to correct weaknesses previously noted in CRA examination reports.

Given that Texas has the nation's lowest average credit score, it is important to address the need for financial literacy education. In 2006, DOB launched a financial education initiative and hired a financial education coordinator to promote financial education throughout the state by holding workshops and helping banks start financial education programs.

DOB plans to hold quarterly train-the-trainer workshops throughout Texas over the next two years as part of this effort. The goal of these sessions is to provide hands-on training to bankers about available financial education curricula and to provide a forum for discussing the current financial needs of Texas residents.

In August 2006, DOB asked all state-chartered banks to complete a survey about their financial education initiatives. The survey results identified a range of financial education programs in place as well as institutions interested in receiving assistance in establishing such programs. The survey found that 86 percent of the institutions surveyed are interested in providing financial education services to community members.[107]

Texas Department of Banking Online Financial Education Survey Results

One hundred fifty-four banks responded to the August 2006 DOB survey. The following summarizes its results.

In 2001, the federal Office of the Comptroller of the Currency enacted a rule allowing national banks to open offices in a school without becoming a branch, if the principal

CHART 1

Does Your Bank Conduct Financial Education Training for Your Community?

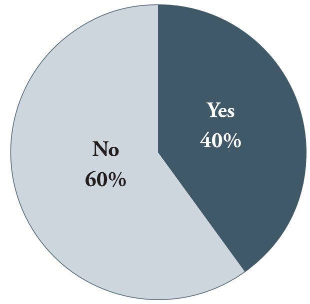
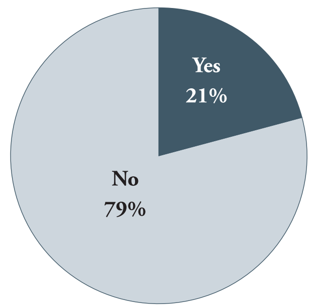


CHART 2

Does Your Bank Have a Person Over Customer Financial Education?



Texas banks clearly need to increase their efforts to provide financial services in Spanish to better serve their communities.

CHART 3

Is Your Bank Interested in Providing Financial Education Services to People in Your Community?

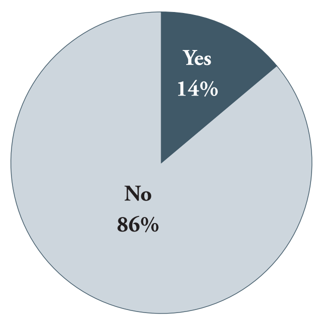
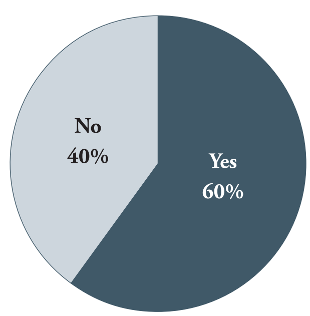


CHART 4

Does Your Company Offer Customer Service in Languages Other Than English?

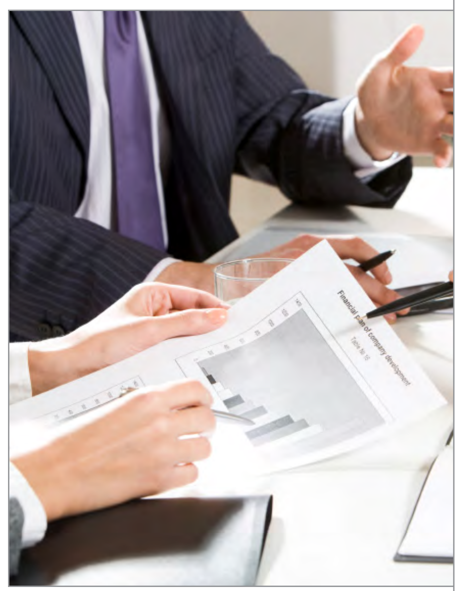


Note: Sixty percent of banks offer customer service in languages other than English. The survey results indicated that the alternate language is overwhelmingly Spanish. According to the U.S. Census Bureau's 2006-2008 American Community Survey, the total population of Texas is almost 23.8 million, of which approximately 8.6 million Texans are of Hispanic origin.[108] Based on these statistics, Texas banks clearly need to increase their efforts to provide financial services in Spanish to better serve their communities.

purpose for the office is educational. In response, DOB coordinated with FDIC to develop a rule that would allow bank offices in Texas schools.

On Sept. 25, 2008, the FDIC adopted a new rule allowing its state non-member banks to open an in-school bank without filing a branch application or seeking prior approval.[109] The rule requires the services to be provided at the discretion of the school and to be for the principal purpose of financial education. The services can include receiving deposits, paying withdrawals and lending money.

The Texas Finance Commission is responsible for overseeing and coordinating the activities of the Texas Department of Banking, the Department of Savings and Mortgage Lending and the Office of the Consumer Credit Commissioner and serves as the primary point of accountability for ensuring that state depository and lending institutions function as a coherent system. The Finance Commission is the policy-making body for those agencies and is not a separate state agency.[110] On Oct. 16, 2008, the commission approved a new rule that is similar to the FDIC rule except that the in-school banks are given a name, COMET (Center of Monetary Education for Texans), and that banks must give DOB 30 days notice of their intent to open a COMET.



Economic Development Strategies

The Governor's Small Business Assistance (SBA) team, within the Economic Development and Tourism (EDT) Division, is charged with identifying legal and financial barriers for small, medium-sized and historically underutilized businesses; assists small and medium-sized enterprises with expansion programs, policies and directives; and develops strategies for small business development throughout the state.

EDT's International Team creates and promotes a business climate conducive for small-business expansion beyond Texas and national borders and encourages and supports relationships between small Texas businesses and international partners. In addition, EDT works with local communities and state agencies, including the Texas Department of Agriculture, Texas Workforce Commission, Texas Commission on Environmental Quality and Texas Department of Transportation, on projects to create jobs and opportunities in Texas communities.

The Governor's SBA office will continue to conduct small-business summits in various Texas cities to allow business owners to meet lenders and learn more about securing financing. It will also provide assistance through the Governor's Web site for individuals who seek information on starting and financing a business. SBA also responds to telephone calls and correspondence from Texas citizens who want to learn more about securing financing.[111]

Housing Strategies

As a result of the nationwide foreclosure crisis, as well as recent natural disasters, TDHCA is developing new programs and expanding existing programs to encourage community reinvestment. The new programs will focus on creating a stable housing market during the foreclosure crisis and developing a housing recovery program for damage caused by Hurricane Ike. The 81st Texas Legislature approved an increase of $21,927,750 in Housing Trust Fund money for the 2010-11 biennium, an increase of 87 percent in funding per year. This will allow TDHCA to create additional programs to reach low-income Texans.[112]

Under Title III of the federal Housing and Economic Recovery Act of 2008, the U.S. Department of Housing and Urban Development created the Neighborhood Stabilization Program (NSP).[113] Through NSP 1, the initial portion of the program, TDHCA will receive about $102 million over 18 months to rehabilitate, resell or redevelop foreclosed properties. This program will stabilize communities by targeting properties that could become sources of blight. The funds must be obligated 18 months from the start of the program, which began in March 2009. Funds will be awarded only to state agencies and local governments; no individuals or nonprofit organizations will be eligible.[114]

TDHCA and the Texas Department of Rural Affairs jointly submitted an application for NSP 2, the second portion of the Neighborhood Stabilization Program, for funding released under the ARRA.[115] Submitted in July 2009, the joint application requested $110 million for activities similar to those allowed in NSP 1. Both agencies will receive notice of their award status in December 2009. NSP 2 will be expended over three years when the program begins.[116]

A preliminary draft report released by the Harris County Housing Authority in October 2008 estimated that Hurricane Ike caused $8.5 billion in damage to homes, apartments and mobile homes. In 2009, the Governor's Office designated TDHCA as the state's lead agency to administer housing recovery funds for Hurricanes Ike and Dolly. TDHCA administers more than $654.1 million in housing funds by awarding 18 subrecipients selected for local housing recovery efforts, awarding subrecipients on a competitive basis for affordable rental housing activities and reserving an amount for TDHCA administration.

During the 81st legislative session, TDHCA submitted a Legislative Appropriations Request for an additional $20 million annually for fiscal 2010 and 2011 for the state's Housing Trust Fund (HTF). The 81st Legislature approved an increase for the HTF, with an allocation of $10,963,875 annually for fiscal 2010 and 2011.

As of October 2009, the 18 locally administered subrecipients have received $562.6 million. Their proposed activities include owner-occupied rehabilitation; single-family and multifamily rental rehabilitation and reconstruction; down-payment assistance to purchase housing in hurricane-affected areas; hiring staff for code enforcement; acquisition buyout activities that will result in green space or recreation areas; and demolition-only activities.

TDHCA had issued one award for the competitive rental housing set-aside as of October 2009. TDHCA will make other recommendations after it completes its reviews. The deadline to apply under the $58 million set-aside for affordable rental housing activities was August 2009. TDHCA received 22 applications requesting a total of $75,755,261.

In 2007, the U.S. Congress passed legislation to create a National Affordable Housing Trust Fund to help low-income households obtain affordable housing. Eligible uses of the National Housing Trust Fund include construction, rehabilitation, acquisition, preservation incentives and operating assistance to facilitate affordability.

During the 81st legislative session, TDHCA submitted a Legislative Appropriations Request for an additional $20 million annually for fiscal 2010 and 2011 for the state's Housing Trust Fund (HTF). The 81st Legislature approved an increase for the HTF, with an allocation of $10,963,875 annually for fiscal 2010 and 2011. Prior to the increase, the HTF was allocated about $5.8 million annually in fiscal 2008 and 2009.[117]

Because it does not have federal restrictions, the HTF can be used to target hard-to-reach populations, including people with disabilities and people living in colonias. The fund can be used to provide homebuyer and rental assistance for veterans; to expand the successful Bootstrap Home Loan Program; to provide homebuyer assistance and barrier removal for persons with disabilities; and to offer gap financing for rural rental development. The HTF is the primary source of funding for the Bootstrap Home Loan Program and the Bootstrap Program's results are reported under the HTF.

To target funds for its programs, TDHCA conducts various housing research and market studies. Texas Government Code §2306.259 established the Affordable Housing Research and Information Program, which requires TDHCA to undertake four activities: periodic market studies to determine the need for low-income housing; research to determine the effect of affordable housing developments on surrounding neighborhoods; research into affordable housing development approaches; and education and outreach efforts that will help the public understand the nature and purpose of affordable housing.

TDHCA received $120,000 annually in state funding in fiscal 2008 and 2009 for these activities. TDHCA dedicated these funds to market studies in the Texas Panhandle, Dallas and the Rio Grande Valley. The Dallas and Rio Grande Valley studies are still under way, while a market study of Parmer, Castro and Deaf Smith counties in the Texas Panhandle was completed by a national real estate research firm and posted online in October 2008. The study includes a survey of the housing stock, interviews with key stakeholders, a demand analysis indicating potential housing opportunities and a general housing needs assessment. It also addresses the need for farmworker housing in each county.[118]

Insurance Strategies

The Texas Department of Insurance's primary community reinvestment goal is making insurance affordable and available to Texans. In pursuit of this goal, TDI has approved new policy forms and endorsements for homeowner and personal automobile insurance, to encourage a competitive market by ensuring that consumers can choose from an array of fairly priced products. (Endorsements are options, generally to add coverage, in an insurance policy.)

Another TDI program, *Helpinsure.com*, is a Web site that provides information to help consumers shop for auto and residential property insurance. Consumers can view and compare sample rates provided by insurance companies, obtain information about companies and agents and learn more about the types of insurance they need to protect family and property. TDI's Consumer Protection Division sponsors educational programs to help consumers determine their available insurance options. It also provides instructions on how to file a complaint if specific products are not offered in a consumer's area.

Other statutory programs help protect consumers from the loss of insurance, even when an insurer becomes insolvent. Most insurance policies are covered by one of the state's guaranty funds, which pay claims for insurers that become insolvent. The funds cover up to $100,000 for individual life insurance and annuity policies and up to $300,000 for property and casualty insurance policies.[119]

Appendix A:
CRA Evaluations

Four federal banking regulatory agencies regularly examine financial institutions using CRA regulations and examination procedures adopted in 1995.

The Federal Reserve Board oversees state-chartered banks that are members of the Federal Reserve System and bank holding companies. The Federal Deposit Insurance Corporation oversees state-chartered banks and savings banks that are not Federal Reserve members. The Office of Thrift Supervision regulates federally chartered savings banks and savings and loan associations, while the Office of the Comptroller of the Currency regulates national banks, federal branches and agencies of foreign banks, their employees, stockholders and agents.

CRA Examinations and Ratings

As of Jan. 1, 2009, institutions accountable to the FDIC, FRS and OCC must be examined under the following threshold requirements:

- "small bank" or "small savings association" applies to an institution that, as of Dec. 31 of either of the prior two calendar years, had assets of less than $1.109 billion.
- "intermediate small bank" or "intermediate small savings association" means a small institution with at least $277 million in assets as of Dec. 31 of both of the prior two calendar years, and less than $1.109 billion as of Dec. 31 of either of the prior two calendar years.
- financial institutions that accept deposits must have less than $1.033 billion as of Dec. 31, 2006 or Dec. 31, 2005 to claim exemption from 2007 CRA data collection requirements as a small or intermediate small bank.

Annual adjustments to asset-size thresholds follow the year-to-year change in the average unadjusted Consumer Price Index for urban wage earners and clerical workers, for every 12-month period ending in November, rounded up to the nearest million. Adjustments for banks are required by the 2005 CRA regulatory amendments; OTS' 2007 CRA regulatory amendments apply to annual adjustments for savings associations.[120]

The FRB allows intermediate small banks to submit CRA data to preserve the option of a large bank exam. Small savings associations may provide the data to the FRB to preserve their option of a large institution exam. Some intermediate small banks might choose detailed CRA reporting as a large bank when its community development loans, investments and services are weak.

Many intermediate-sized banks lack records of community development loans due to competition for making such loans by competing larger banks in their communities. Also, the intermediate-sized banks may not have adequate records or a formal data collection process to track their community development activities and related loans. Furthermore, it may be easier for intermediate-sized banks to report their lending and investment activity as a large bank to avoid having to learn the new CRA rules for mid-sized banks, particularly if they expect to soon grow above the $1.033 billion threshold and become subject to large-bank exam rules.

Large bank examinations include three tests.

1. A *lending test* represents about 50 percent of the CRA bank examination and uses data from the Home Mortgage Disclosure Act and CRA disclosure statements. Organized by bank and metropolitan statistical area, the lending test also evaluates the number and amount of community development loans. Investments that qualify for CRA lending test credit include lawful investments, deposits and membership shares or grants with community development as their primary purpose.
2. A *service test* evaluates the public's accessibility to the bank's financial and community development services. Banks may submit a strategic plan for the approval of their regulatory agency. Banks that are not in the business of extending home mortgages, small business loans, farm loans or consumer loans to retail customers and that have been designated as a wholesale bank by their primary regulator take a limited CRA exam.
3. The *investment test* examines a bank's record of helping to meet the credit needs of its assessment area through qualified investments that benefit its area or a broader statewide or regional area that includes the bank's assessment area. This test excludes activities already considered under either the lending or service tests. At the bank's option, OCC will consider a qualified investment made by an affiliate bank when the investment is not already claimed by another financial institution.

The CRA allows a bank to apply to its federal regulator to be evaluated under a strategic plan. This option allows the bank to link its CRA objectives with the needs of the community and its own business capacities, goals and expertise. The specific contents of a strategic plan and OCC's criteria for evaluating these plans are found in 12 CFR §25.27 of OCC's CRA regulation.[121]

Regulatory agencies do not award any particular amount of CRA "credit" for a specific financial or community development service. Large financial institutions may receive CRA ratings of outstanding, satisfactory, low to satisfactory, "needs to improve" or substantial noncompliance.

Appendix B:
2007-2008 Changes to the Home Mortgage Disclosure Act

The Federal Reserve Board finalized changes to the Home Mortgage Disclosure Act in 2007 and 2008. Originally implemented by the Federal Reserve Board under Regulation C, the Home Mortgage Disclosure Act requires that certain financial institutions, including banks, credit unions, savings associations and other mortgage lenders, report public loan data to their respective supervisory agencies so that it can be used to determine whether financial institutions are serving the housing needs of their communities. Regulation C applies to savings associations, credit unions and mortgage lending institutions.

- From Jan. 1, 2003, the FRB required lenders to ask applicants their national origin or race and sex on loan applications taken by telephone. The telephone application rule now applies to mail and Internet applications as well.
- Beginning in 2004, Regulation C requires lenders to collect and report additional data on home loans and financing for manufactured homes, including loan pricing information and lien status (secured by a first or subordinate lien or unsecured).[122]
- Beginning in 2004, Regulation C began requiring HMDA and CRA reporters to use new geographic statistical area designations provided by the U.S. Office of Management and Budget on June 6, 2003 when reporting data. OMB's revised metropolitan statistical area boundaries led to changes in definitions updated in February 2004 and effective December 2003. Only the terms MSA (used in place of metropolitan area) and MetroDivs (metropolitan divisions) will be recognized for HMDA and CRA reporting.
- Also starting on Jan. 1, 2004, the FFIEC required lenders to use the five-digit number assigned to MSAs, rather than the previous four-digit number, when collecting and reporting HMDA data.[123] For non-depository lenders, effective Jan. 1, 2004, Regulation C began requiring a $25 million volume test in addition to the existing percentage-based coverage test for mortgage bankers that make at least $25 million in mortgages annually.[124] For 2004 data collection, the asset threshold for depository lenders was raised to $33 million, from $32 million, and remained unchanged at $10 million or less for non-depository institutions. FFIEC uses loan data submitted under the HMDA to create reports for each metropolitan area in the U.S. In 2004, about 8,121 financial institutions provided a total of 42 million loan records for calendar 2003.
- The FRB raised the asset exemption threshold for depository institutions to $35 million in December 2005 for 2006 data collection, but left the threshold unchanged for nondepository institutions.
- In December 2006, the FRB raised the asset exemption to $36 million for 2007 data collection. FRB left unchanged the threshold for nondepository institutions for 2007 data collection, at $10 million or less when combined with a parent corporation's assets or if the institution originated 100 or more home purchase loans in a year, including the refinancing of home purchase loans. Nondepository institutions may combine their assets of parent corporations in the preceding calendar year.

- FRB amended revised Regulation C reporting rules for price information on higher-priced loans as of Oct. 1, 2009. The final rule requires compliance for loan applications taken on or after that date and loans closing on or after Jan. 1, 2010, regardless of the application date. The FRB also lowered the reporting rate spread to 1.5 percentage points on first-lien loans and 3.5 percentage points on subordinate-lien loans.[125]
- On Dec. 18, 2008, FRB increased the asset-size exemption for depository institutions to $39 million, based on the annual percentage change in the CPI for urban wage earners and clerical workers, for the 12-month period ending in November 2008. This change exempted depository institutions with assets of $39 million or less as of Dec. 31, 2008 from collecting data in 2009.[126]

Appendix C:
Update of the *Study of Residential Foreclosure in Texas*

This section updates the original *Study of Residential Foreclosure in Texas* submitted in 2006 by the Texas Department of Housing and Community Affairs in response to House Bill 1582, 79th Legislature, Regular Session. TDHCA examined mortgage foreclosure activity and trends in Bexar, Cameron, Dallas, El Paso, Harris and Travis Counties.

Foreclosure and Delinquency Rates

According to data from the Neighborhood Stabilization Program, a HUD-funded program to acquire and redevelop foreclosed properties that may become abandoned and lose value, Texas' statewide foreclosure rates averaged 3.7 percent during the 18 months preceding December 2008. The program counted the number of estimated mortgages in the state and foreclosure starts during the 18 months prior to December 2008.[127] RealtyTrac reported that a total of 96,157 residential property foreclosure notices were filed in Texas during 2008. This represented a 13.8 percent increase from 2007 and a 15.0 increase from 2006.[128]

A December 2008 study by the Mortgage Bankers Association ranked Texas in the top 10 states for late loan payments. During the third quarter of 2008, 8.4 percent of Texans were behind one month or more on their mortgage payments, compared with 7 percent of homeowners nationwide. According to this study, 29 percent of Texas mortgage holders had nonprime loans, compared with 19 percent nationwide; the subprime mortgage delinquency rate in Texas was 18.2 percent.[129]

Alternatives to Foreclosure

Fannie Mae's *Study of Residential Foreclosure in Texas* defines foreclosure as the "borrower's actual loss of the home as the final result of a legal process that was preceded by borrower default on the loan."[130] Foreclosure *rates*, however, are difficult to quantify. Various data sources count foreclosure as beginning at different points in the foreclosure process. For example, RealtyTrac includes foreclosure *notices* in the foreclosure rates, while the *Study of Residential Foreclosure in Texas* includes only the actual loss of a home in foreclosure rates. Foreclosure is a process and not all foreclosure starts actually end in foreclosure.

Although the first missed mortgage payment is a breach of the agreement between the homeowner and the lender, the foreclosure process usually begins when the homeowner misses three or more payments. According to NeighborWorks America, during the foreclosure process the loan is deemed either curable or incurable. Established by Congress in 1978 as the Neighborhood Reinvestment Corporation and renamed NeighborWorks in 2005, this national nonprofit promotes reinvestment in older neighborhoods and provides financial support, technical assistance and training for community-based groups. Revitalization of older areas includes repairs to distressed apartment buildings and shopping areas, promotion of homeownership and training jobless youth in home construction.

Curable loans are usually characterized by three factors: homeowners' desire to remain in their home; a resolution of the financial crisis that caused the missed payments; and the homeowners' ability to maintain and afford payments over the long term. Curable loans will lead to reinstatement options that allow the homeowner to maintain ownership.

Incurable loans lack one or more of these factors, and often result in disposition options other than foreclosure in which the household does not maintain ownership of the home.

Reinstatement options for curable loans include six measures: repayment plans, loan modifications, reverse equity mortgages, forbearance, partial or advance claims and mortgage refinance. A *repayment plan* is used when the financial crisis has been resolved and the homeowner can afford to pay extra each month to catch up on missed payments. A *loan modification* is a written agreement that changes the original terms of the loan, such as by reducing the interest rate or adding the total delinquent amount owed to the balance of the loan. A *reverse equity mortgage* is, as the name implies, a reversal of mortgage payments; the homeowner can live in the home for the rest of his or her life while a bank buys the equity in the home. This option can be used by homeowners who are 62 years or older and have significant equity in their homes.

The remaining reinstatement options are used less frequently. *Forbearance* is an agreement to suspend or reduce payments for a fixed period of time; at the end of the period, the deficiency is cured with a lump-sum payment.

The *partial* or *advance claim* option requires an investor or mortgage insurer to advance funds to reinstate the loan. A partial claim represents an additional risk to the servicer because, if the homeowner defaults, the amount of the advance is subtracted from the servicer's claim.

For a *mortgage refinance*, the homeowner must have equity in the home and good credit to pay off the existing loan by taking out a new loan with the same property as security. A new loan may have a lower interest rate or fixed rate that will lower the homeowner's payments. Often, any missed payments that resulted in the original delinquency negatively affect the homeowner's credit score, so that refinancing is impossible because the homeowner does not qualify for a new loan.

Even when a loan is incurable, four disposition options are available to the homeowner other than foreclosure. These include selling the property; a hardship mortgage assumption; a short sale (also known as pre-foreclosure sale or short payoff); and a deed in lieu of foreclosure.

While *selling the home* may be difficult for the homeowner to accept, it may be a viable option if there is sufficient equity in the property to cover selling costs. If the home has enough equity, the sale of a home may yield a lump sum for the homeowner and help him or her start fresh in a new location. A *hardship mortgage assumption* occurs when a qualified buyer assumes the title and mortgage obligation of a borrower in default. A *short sale* occurs when a property is sold for less than the total loan amount due. A *deed in lieu of foreclosure* calls for the homeowner to voluntarily convey title to the servicer in exchange for discharge of the debt.

Due to high national foreclosure rates, loan holders such as Fannie Mae have added additional, nontraditional measures to help homeowners avoid foreclosure. Fannie Mae has created a streamlined loan modification program that allows borrowers who have missed three payments to more easily modify their loans. It also has created new servicer guidance that allows foreclosure prevention tools to be used before a homeowner is delinquent. In addition, the agency has created an "early workout" program that permits servicers to pre-negotiate a loan modification that becomes permanent only after a trial period proves effective for the homeowner. Furthermore, Fannie Mae has doubled the forbearance and repayment plan periods for most loans. Finally, a 2009 single-family master trust agreement allows servicers for Fannie Mae to modify a loan after one month of delinquency if it meets certain criteria.

Homeowners who owe more their homes than their homes are worth may be able to refinance or modify their existing mortgages under Making Home Affordable, a plan introduced by the Obama Administration to stabilize the U.S. housing market and help qualified homeowners reduce their monthly mortgage payments to more affordable levels. To refinance the mortgage, homeowners must not have been more than 30 days late on their mortgage payment in the last 12 months; must occupy the home as a primary residence; must have a mortgage through Fannie Mae or Freddie Mac; and must owe more on the mortgage than the current market value of the home. To adjust the mortgage, homeowners must have had trouble making the mortgage payment due to an increase in the mortgage payment or reduction in income or other hardship that increased expenses; occupy the home as a primary residence; owe less than $729,750; and have received the current mortgage before Jan. 1, 2009. This program expires June 2010.

When homeowners in default are considering a reinstatement or disposition option, they should be aware of scams targeting people in danger of foreclosure. Such schemes already have been identified in Texas. In 2008, Texas Attorney General Greg Abbott helped to shut down Foreclosure Assistance Solutions LLC of Florida and its principal operators for falsely promising to work out a solution between homeowners and their mortgage companies.[131] Any foreclosure mitigation should be conducted directly with the mortgage company or with a HUD-approved housing counselor, or after consulting Legal Aid of Texas.

Texas Department of Housing and Community Affairs Response to Foreclosures

Foreclosure may be prevented if the homeowner receives assistance during the foreclosure process. TDHCA has taken several steps to provide relief for homeowners in danger of foreclosure and neighborhoods with high foreclosure rates. The agency has resources listed on its Web site at www.tdhca.state.tx.us/homeownership/foreclosure that provide useful information to homeowners in danger of foreclosure. TDHCA also has become involved in the Texas Foreclosure Prevention Task Force and administers the National Foreclosure Mitigation Counseling program in Texas as well as the Neighborhood Stabilization Program.

In 2007, TDHCA became one of the founding entities for the Texas Foreclosure Prevention Task Force (TFPTF), which currently has 90 members. TDHCA coordinated six press events viewed by 21 percent of all Texans between March and June 2008 to announce TFPTF's launch. The task force's mission is to reduce residential foreclosures and the impact of foreclosure on neighborhoods. Its main goals are to conduct outreach, perform research and develop a source of funds for foreclosure prevention.

By conducting outreach, TFPTF links struggling homeowners to counseling services. In cooperation with NeighborWorks America, a national nonprofit organization created by Congress, and the HOPE NOW Alliance, a national homeownership preservation initiative, TFPTF participated in free foreclosure intervention workshops in

Arlington and San Antonio during June 2008. More than 600 families received housing counseling and spoke directly with their lenders at these events. TFPTF also works with the HOPE Hotline, a national hotline that connects homeowners with housing counselors.

TFPTF's research involves monitoring mortgage default patterns; collecting information about mortgage assistance programs; analyzing potential legislative recommendations that support homeownership retention; and developing a tracking system to measure the effectiveness of TFPTF activities.

To meet its financial goals, TFPTF raises funds to provide training to counseling organizations and to reimburse counselors for their services. Since its inception, TFPTF has raised more than $400,000 from various sources including corporate and private foundations, banks, nonprofit organizations and TDHCA.

The federal Housing and Economic Recovery Act (HERA) of 2008 resulted in two foreclosure-related programs now administered by TDHCA: the National Foreclosure Mitigation Counseling Program and the Neighborhood Stabilization Program.

HERA authorized NeighborWorks America to administer the National Foreclosure Mitigation Counseling (NFMC) Program. NFMC is intended to expand and supplement foreclosure counseling offered by HUD-approved housing counselors. Eligible recipients of foreclosure intervention counseling must be owner-occupants of single-family (one- to four-unit) properties with mortgages in default or danger of default.

TDHCA partnered with HUD-approved counseling organizations to create an application for NFMC funding. In December 2008, TDHCA received the NFMC award notification and will receive $491,490 for foreclosure intervention counseling, training and administration expenses that must be used by Dec. 31, 2009. The funds will support 949 additional foreclosure-counseling sessions in Texas.

TDHCA will jointly administer the NFMC program with the Texas State Affordable Housing Corporation (TSAHC), a not-for-profit organization. All NFMC funds will target "areas of greatest need," defined by Neighbor Works as areas experiencing a high rate of sub-prime lending, delinquent loans and foreclosure starts. About 30 percent of the funds will be targeted to low-income or minority homeowners and neighborhoods.

In August 2009, TDHCA and partner HUD-approved counseling agencies submitted an application for about $945,000 in additional NFMC funding. If awarded, the additional funding will provide about 3,530 counseling sessions to homeowners in danger of foreclosure.

HERA also created the Neighborhood Stabilization Program (NSP) 1, a HUD-funded program that will redevelop abandoned and foreclosed properties into affordable housing or acquire and hold them, in areas documented to have the greatest need for assistance due to declining property values caused by excessive foreclosures. TDHCA will administer this program. Units of local governments and other entities, with the consent of the appropriate local governments, can apply for these funds.

TDHCA, TDRA and TSAHC will work together to administer $102 million in NSP 1 funds. TDHCA is taking the lead role in this partnership. It proposes to use $51 million for direct awards, $31 million for a select pool, $10 million for a land bank administered by TSAHC and $10 million for administration.

The select pool is an amount allocated for counties that did not receive a direct award through the Texas NSP 1. The select pool counties or entities within those counties applied in April 2009 for funding from the select pool. The land bank allows nonprofits or local governments administering the NSP 1 program to purchase properties and hold the properties up to 10 years before transferring them to their final eligible use.

Each recipient of NSP 1 funding will be required to target at least 35 percent of its non-administrative allocation to benefit households with incomes less than or equal to 50 percent of the Area Median Family Income. Acquisition of real property by NSP 1 administrators allows recipients of NSP 1 funds to purchase the abandoned or foreclosed properties to rehabilitate and sell to households earning 120 percent of the AMFI or less.

The ARRA extended the Neighborhood Stabilization Program, creating another round of funding for the program known as NSP 2. TDHCA and the Texas Department of Rural Affairs (TDRA) jointly submitted an application for NSP 2 to HUD in July 2009. The application requested $110 million for activities similar to those in the NSP 1 application. The only activity not included in NSP 2 is land banking. The departments will be notified of their award status in December 2009. NSP 2 funding will be expended over three years, after the program begins.

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